Furious Gold

Marxist Essays on the Theory of Money

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'But silken nets and traps of adamant will Oothoon spread, And catch for thee girls of mild silver, or of furious gold' – William Blake, *Visions of the Daughters of Albion* (1793)

Cover image: a detail from the tetraptych altarpiece in Sankt Annenkirche in Annaberg, by Hans Hesse, 1523. The paintings of Hesse depict the various occupations in the silver mining industry of Bohemia, which played an important historical role as mentioned in Kautsky's 1913 booklet included in this volume.

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Published on Internet Archive (archive.org), March 2025.

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Introduction

The 1880s saw the invention of improved methods of gold extraction. Reporting on one such method,[1] Kautsky concluded:

> … The consequences that this huge increase in gold production will bring about must be significant. The regime of dual currency will become untenable once the current ratio of gold value to silver value shifts considerably; the fall in the value of gold will allow the transition to a pure gold currency without sacrifice.[2] The victory of the gold currency[3] will thus be just a matter of time. However, the increase in gold production will also powerfully promote the industrial development of America, Australia, India and South Africa, and make their competition with the industry and agriculture of Europe still more devastating. Finally, the increasing devaluation of gold must result in price increases of all other commodities, thereby compelling the workers to demand a proportionate increase in wages. Wages, however, follow but reluctantly the growth in commodity prices … [I]n all branches this devaluation must result in fierce and bitter wage disputes; because no matter how much the prices of commodities rise, even the slightest wage increases can almost never be wrung from the capitalist without a fight.
>
> Thus a new factor is joined to the existing factors of unrest and unease in contemporary society – overproduction, overseas food competition, the disintegration of the petty bourgeoisie and the small peasant class, and so on –: *the devaluation of gold*.

The rise of prices began in the mid-1890s. The immediate question in the debate among Marxists, which is translated here, was whether gold production had been a cause.[4] Kautsky

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[1]Kautsky 1884. The description was copy-translated from an anonymous article in *The Journal of science*. The MacArthur-Forrest process (cyanidation) dates from 1887. See Lafargue 1908.

[2]Kautsky means here that the debtors' plight will not be worsened. The value ratio between silver and gold did widen, as noted by Engels in the 1890 edition of Capital (Marx 1976, p. 241). Engels was apparently still unaware of the improved methods of gold extraction, since he claimed that the labour expended on the production of gold was tending to rise.

[3]*Goldwährung* is often translated as 'gold standard', but *Währung* means money, so here we will use 'gold currency' for lack of a better term ('currency' being still not exact). The original meaning of 'standard' (in English) refers to a certain fineness (Chaffers 1905, p. 47). A 'standard of price' or standard of money is a fixed weight of metal defining one money unit; gold itself does not have a price, but *is* the price (of commodities). It is constantly confused with money's function as measure of value (Marx). One can speak of the 'gold measure' (of values).

[4]It constitutes part two in this volume. Among the commentators on the debate is for example Evgeny Preobrazhensky (forthcoming translation in volume three of his *Papers*). A critical chapter in Berkovsky 1930a.

affirmed so:

> I attribute the rise in the cost of living during the last two decades before the war to two main causes: 1) The depreciation in the value of gold, due to the decrease in the cost of its production. 2) The exhaustion of the immense regions of woodland and prairie in America and other new countries which were originally under no restrictions of private property.[5]

Varga and Hilferding did not regard it as a cause, though needless to say, that was not intended as an apologia for gold currency.

'Restricted' or 'blocked' currency (*gesperrte Währung*)

To cope with the increased gold production some toyed with the idea of a restriction of gold coinage:

> ... under a system of gold currency in which free coinage (that is, the right of individuals to have their gold coined at any time) has been discontinued, the value of coin can increase in terms of uncoined bullion. ... Its explanation by modern economists is still awaited with great impatience. The idea of suspending free coinage was under discussion in England in the middle of the 1890s when gold production rose rapidly, the supply of money increased ...[6]

Marx was attacked on the grounds 'that free coinage, upon which he bases all his discussion of money, is no more a natural system of money than capitalism is the natural and eternal system of economy'.[7] 'Restricted' coinage (*gesperrter Prägung*), that is the blocking of the

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In English there is Levy 1982 (see additional materials to this volume: http://libcom.org/library/furious-gold), and briefly in Mommen 2011.

[5]Kautsky 1920, p. 106. Though by 1906 the nature of the rise in prices had changed (Kautsky 1913).

[6]Hilferding 1981, pp. 56, 382. Free coinage of gold existed, although the right was rarely made use of. In Britain the last occurrence was in the 1870s when an MP for Great Grimsby as an experiment sent an ingot of gold to the mint. It also seems that the mint was not obligated to accept orders for less than £20000. By 'free' is meant 'unrestricted'. When coinage is without charge it is called 'gratuitous'.

[7]Hitch 1900, p. 33. Marcus Hitch (1855–1926) held to the quantity theory of money as 'a self-evident truth'. See the reply by N.I. Stone, also in *International Socialist Review*. It was this article, as Stone recounts in a 1912 letter to Kautsky, that led him to translate Marx's *Zur Kritik* (1859), initially wanting to change the title to *Money*, because 'it more correctly describes the real contents of the book ... [and] would lend the book a more wide spread popular interest, than the more abstract sounding [*A Contribution to the*] *Critique of Political*

public's access to the mint, had already befallen silver, so to some it then seemed possible also for gold. Hilferding theorised that under such a system, or in general under 'paper money', the value of currency would be directly determined by that of the commodities, and no longer solely that of gold. This theory was rejected by many Marxists, starting with Kautsky.[8] Hilferding did not respond to Kautsky's criticism, yet his theory remained influential.[9] Kautsky himself appears to have accepted it in 1918 for 'paper money'. Due to this cessation of the debate, not everything has become clear about Hilferding's terms, such as for instance paper money. Restricted coinage (of gold) and 'paper money' are two different things, but he speaks of them in the same breath.[10] What they have in common, and what actually matters in Hilferding's scenario, is the refusal of the monetary authorities to accept gold bullion for conversion into either gold coin or 'paper'. It entails on the other hand, of course, also the refusal to convert paper into bullion, and the refusal to convert gold coin (which still can circulate under this 'paper money', only now as a token coin) into bullion (the latter appears difficult to prevent, as anyone can melt coins).

So when Hilferding speaks of 'paper money' he assumes that also the coinage of gold is blocked. That is, if there is not this restriction on coinage, his theory does or cannot apply. Moreover, the monetary authority's suspension of convertibility of paper into gold does not have to coincide with its refusal to convert gold into paper. Historically there were many suspensions of paper convertibility, but they went along with free coinage, and with the continued conversion of gold into paper. For example Britain in 1797–1821. The Swiss central bank after the first world war did refuse to 'buy' gold with paper, but coinage remained free (this example to be seen in more detail later).

And when Hilferding speaks of restricted coinage of gold, he also assumes the central bank's (or state's) refusal to convert gold into paper. That is, if coinage is restricted, but gold

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Economy' (Stone 1903).

[8]Riazanov congratulated Kautsky for his critique of it, though he disagreed about gold's role in the price increase, nitpicking on Kautsky's 1913 brochure. Laurat in 1934 wished for its republication and likely discussed it in his unpublished book *La valeur de l'or et le mouvement des prix à l'époque des monopoles* (Laurat claimed that Bauer was prevented from solving the gold issue by a confusion of the phenomenon of the equalisation of the profit rate between branches with its differentiation within each branch). Lenin referenced Kautsky's critique, for example in comments on Hilferding's *Finance capital*. In a review of the latter work even Bernstein (1912) objected that paper currency without a relation to money metal presupposes an economy radically different from capitalism, only thinkable in a certain stage of communism. On the price increase however, Bernstein did not believe it was due to the decline in gold's value, rather he endorsed the quantity theory (that is, due to the increase in gold's quantity).

[9]Hilferding's theory influenced Herman Cahn, author of *Capital today* (1918). Cahn did attribute the rise of prices to a fall of gold's value (pp. 103–5). He argued that capitalism would collapse due to contradictions inherent to money.

[10]Perhaps due to the accidental and inconsequential situation in 1880s Austria-Hungary where the restriction of silver coinage just happened to go along with the suspension of convertibility of paper into silver. Nobody would have been tempted to use this right of convertibility anyway if it had existed.

continues to be accepted for conversion into paper, again his theory cannot apply. For example Britain in 1925–31.

If even restricted coinage is finally abolished (that is coinage as such is abolished), but the central bank or state continues to convert ('buy') all gold offered to it into paper, as was the case in the United States after 1933, we would argue that Hilferding's theory still cannot apply. There was no restriction of the currency supply, anyone who offered gold would get (new) dollars.[11] It could also be withdrawn from (world) circulation, it was convertible into gold bullion (not into gold coin). It seems we can classify the dollar at that time as an 'unrestricted' currency: no obstacle for anyone to expand note circulation and no obstacle to decrease note circulation.

Has the dollar become a 'restricted currency' (*gesperrte Währung*) now that the US Treasury discontinued both these facilities? The answer hinges on the activity of the central bank. Only the monetary authority could decide whether to block or unblock the decrease and increase in the amount of legal tender notes. Commercial bullion banks cannot keep gold accounts at the Federal Reserve, which thus cannot lend out gold. The Fed also still is legally prevented from accepting gold bullion as eligible collateral.[12] But if it was granted this right, why would the Fed policy-wise choose not to use it, that is allow an unrestricted or free currency?[13] Surely when banks need new dollars they prefer to 'loan' (actually sell in a repurchase agreement) to the Fed their barren gold, instead of their interest bearing securities. Though then again, there is no need for banks to 'sell' gold to the Fed in particular, since it is willingly absorbed by the market, whereas securities might not always be. The 'demand' (to use Hilferding's inappropriate term) for gold still is unlimited.[14] The same option of selling gold on the market, instead of directly to the central bank, existed in the past, but was set aside in the debate on gold. Rightly so, because this procedure does not

[11]See note 31. Less extreme than complete refusal to purchase gold, but of the same principle as restriction, is the lowering of the purchasing 'price' (taking away the floor). Such proposals were made even into the late 1960s (Piquet 1968, pp. 151ff.). Kriz, gold expert at First National City Bank of New York, a bank licensed to deal in gold abroad, called it 'a hollow threat'. But even were it realisable, he claimed that 'it would tend to appreciate the dollar against other currencies once foreign governments and central banks had exhausted their dollar reserves and available dollar credits. An appreciation of the dollar would make it more difficult for the United States to sell its exports ...' (Kriz 1967, p. 23).

[12]However, to foreign central banks it can extend gold-secured loans. Annual reports of the Fed until 1970 mention the use of this gold loan facility. Meltzer also remarks that, '[o]ne of the ways in which the New York bank worked with the BIS was making short-term [collateral] gold loans' (Meltzer 2010, p. 218). The Central Bank of Russia today does accept gold as collateral from commercial banks.

[13]The Federal Reserve today in practice does not discount for example bills of exchange and bankers' acceptances either (LaRoche 1993), but nobody would claim that therefore these are no longer forms of (credit) money. Likewise for their lack of legal tender status.

[14]It is wrong to imply though, as Mandel does, that only now the 'demand' for gold has become unlimited: 'Once the central banks stopped buying current gold production at a price fixed in advance, gold-the-universal-equivalent became a commodity that in any quantity automatically found a buyer in the market' (Mandel 1980, p. 121).

create new legal tender currency, which is the prerogative of the central bank (or mint). If a central bank does not accept gold as collateral (or itself 'loan' gold to the market and thus withdraw notes), then by definition the currency can be called restricted or blocked. Hilferding seems to imply that the central bank thereby gains control over the quantity of currency, just like with its power to decide on the purchase or sale of securities.[15]

Perhaps some would unceremoniously ignore the precondition for the application of Hilferding's theory, and propound the theory on its own merits. Abandonment of Marx's money theory, also when couched within a doctrine of the decline of capitalism, by default leads to some variation of Hilferding's theory. The Marxist polemic against the latter therefore remains necessary.

Worst mine

Another subject in the debate (Kautsky–Varga) that is still with us, concerns the particularity of gold production. Kautsky criticised Varga's position, accepted also by Otto Bauer, that gold's value is determined by the least productive mine. Kautsky noted Marx's rejection of this position, that had been put forth already by Ricardo. Later Keller, while accepting this position, rejected Varga's claim that gold's value remains unchanged (under a fixed conversion rate) when labour expenditure decreases (for Varga merely the differential rents increase).[16] Mandel too accepted it, at least for the era without a fixed conversion rate.[17] He took this position to its conclusion, namely, that when the 'gold price' rises the exploitation of new, worse mines begins,[18] hence the value of gold increases. It seems this would bar even the possibility of gauging the depreciation of the dollar in terms of gold.

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[15]This refers to base money, not control over the total amount of (commercial) deposits. 'The same pieces of money can serve as instrument for any number of deposits' (Marx 1981, p. 603). The central bank theoretically could decide to close its discount window (or standing lending facility).

[16]Vladimir Keller (1898–1954), economist, literary critic. Keller tried to solve a problem, recapitulated by Katzenelenbaum (1921), that plagues this position: When the needs of commodity circulation change, say, require more gold, gold production will increase. But that means the exploitation of new, worse mines, that is the value of (including the already existing) gold increases. But if so, then society requires a different (lesser) quantity now to fulfil its same needs of commodity circulation, than according to gold's old value. There emerges the vicious circle: value of money metal – labour expenditure on the worst mine – amount of metal, necessary to society – value of money metal. The solution which Keller tried to find, unsuccessfully according to Katzenelenbaum, is that there will be established an equilibrium in the middle (Keller 1925). A good point in Keller's article is his criticism (of Bauer's acceptance) of Varga's claim about a lack of internal competition in the gold industry.

[17]See Mandel 1980, and 1984, p. 148.

[18]For example the mining history of Carlin, Nevada (see Malozemoff 1990).

Forced currency

Another important point is whether today's inconvertible currency is subject to either the laws of state paper money or still those of the banknote (credit money). In the Hilferding–Kautsky debate the term 'paper money' was used in the loose sense of inconvertible currency, thus ignoring the distinction between state paper money and inconvertible banknotes. Banknotes were the dominant currency then, based on the discount of bills of exchange. Both Kautsky and Hilferding assumed that when banknotes are declared inconvertible, they become subject to the laws of state paper money. Other Marxists insisted that inconvertibility of the banknote as such does not erase its distinction from state paper money.[19]

State paper money was literally forced into circulation by the state as payment for its expenses, whereas banknotes were not expended as a payment, but *voluntarily* taken up as a loan based on the requirements of circulation, which had to be repaid, that is, returned to the issuer. Banknotes thus are not forced to stay in circulation, they have a regular reflux. In contrast, the state paper money does not have to be returned. A reflux of state paper money would require taxes specifically to be paid in paper, whereupon the paper withdrawn from circulation would have to be destroyed by the state.

> In Prussia there is paper money with forced currency [*Zwangskurs*]. (A reflux is assured for it in so far as a proportion of taxes must be paid in paper money.) These paper thalers are not drafts [*Anweisungen*: instructions] on silver, they are not legally exchangeable [*legal austauschbar*] for it at any bank, etc. They are not loaned by any commercial bank against bills of exchange, but are paid out by the government to meet its expenses. But the notes are denominated in terms of silver. A paper thaler is supposed to represent the same value as a silver thaler.[20]

It is possible that Marx used the word *Zwangskurs* as German translation for the concept of forced currency ('forced paper money', 'paper money which a government compels the

[19]Finn-Enotaevsky, Berkovsky 1930a, pp. 52–9, Schtejnschlejger 1939.

[20]Marx 1986b, p. 70. In a comment on Prussian paper thaler in *A contribution* he calls it *gesetzlich inkonvertibel*, but in fact this Prussian state paper money (*Kassenanweisung*) was convertible on presentation at the state treasury. It was not legal tender in private transactions, which is why Marx observed that private banks had no obligation to accept it for exchange into silver. The chapter on money in the Grundrisse (Marx 1986b, 51–170) was first discussed by Leont'ev (1932) and Broński (1936).

people to receive', 'compulsory government paper') found in British political economy, that captures this difference between paper and credit money.[21] But the word has other meanings.[22] In his analysis of coin and tokens of value, Marx alludes to state paper money with forced currency, which in the usual English translation of *Capital* is rendered as both legal tender and inconvertible.[23] In *A contribution* Marx writes that 'state paper money with forced currency is the perfected form of the token of value'.[24] There is no reason to understand Marx to be referring precisely or only to inconvertible paper money. Granted, it seems that convertible (on presentation) state paper money was uncommon prior to the nineteenth century (a possible case being the Austrian bancozettel 1770s–1800).

This form of state paper money later appeared in German states. Other examples; The Russian money reform in 1897, which made the state paper money (confusingly called state credit notes) convertible into gold. Here the point is that this did not transform its character into that of a banknote as prevalent in Western Europe.[25] In the United States the Treasury issued convertible gold certificates. As Cahn (1918) analysed, even before the war these were being concentrated in the reserves of the banks, probably also helped by the fact that they were not legal tender until 1919. After 1933 they, along with gold coins, were withdrawn from domestic circulation, but they continued to play a role in the Federal Reserve system.

Hoarding and “hoarding”

Although not for the same reason, Hilferding and Kautsky[26] insisted on the difference between private hoarding (for example gold's transformation into luxury articles) and bank hoarding of gold (we leave aside allocated accounts). At first sight gold seems to be withdrawn from circulation in both cases, with Kautsky focusing primarily on the former, Hilferding on the latter.

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[21]For example Simon Gray (of Dunse, Berwickshire) 1815 (written 1804), pp. 171–2, Thomas Smith 1807, later more famously Tooke and Fullarton.

[22]The correct meaning of the German word *Zwangskurs* is, that a person payed in money of this status cannot refuse to accept it, that is, cannot go to court and demand payment in for example silver coin instead. The payment is considered legitimate (legal tender). *Zwangskurs* had a second, the commonly used meaning, that of inconvertibility. In French there are different words: *cours legal* (legal tender) and *cours forcé* (inconvertible). But they too were commonly used with the incorrect meaning (*cours forcé* to describe legal tender). English translations of Marx sometimes even did not use either of these two meanings, but phrases like 'legal rate (of exchange)' and so on.

[23]Marx 1976, p. 224.

[24]Marx 1987, p. 350 (our translation). 'Staatspapiergeld mit Zwangskurs ist die vollendete Form des Wertzeichens'.

[25]This is argued by Finn-Enotaevsky 1911, p. 185.

[26] Kautsky 1913, section 3 towards the end.

This distinction can perhaps be illustrated with a circumstance that arose in the United States in the 1930s. Between 1931 and September 1936 gold mine output (excluding USSR) totaled $4,713 million. Individually owned gold in western countries increased by $3,452 million (American citizens could own gold abroad). If this gold was held in banks, we should thus classify it as bank hoarding. In the following period from October 1936 to June 1937 $1,217 million of this gold was 'dishoarded', accounting for over half the increase in central gold reserves ($2,177 million) during the same period.[27] Since these official reserves normally are also part of the banking system, there was no real dishoarding, just a shift in ownership. When however the Treasury at this particular moment (December 1936 to April 1938) sterilised the gold accruing into its reserves (that is kept it out of the banking system), we could classify that part of its reserves as private hoarding, even though it was owned by the state. Overall for the 1930s though, there was an increase of bank hoarding.[28] Mandel referred to this situation in a criticism of Kautsky:

> Kautsky overlooked the fact that an increase in the *volume* of gold production leads only to an increase in *money* capital, and the distinctive characteristic of gold is precisely that it does not have to be injected into circulation, but can also be hoarded in the form of treasure. There is hence no automatic certainty - as Kautsky assumed - that the annual production of gold will raise the total demand for commodities along with its own value. This depends on whether or not the additional quantity of gold is integrated into circulation, i.e., on the given conjuncture of the capitalist economy, the volume of commodity production, the velocity of the circulation of money, the volume of credit (the payments, besides the exchanges functions, which have to be met by this money) and so on.
>
> Between 1929 and 1939 gold production nearly doubled without significantly increasing total demand in the capitalist world. The additional gold flowed into the currency reserves of the USA and *was hoarded*. Only a reduction in the *value* of gold automatically leads to an increase in the prices of commodities expressed in gold. It is precisely the reduction in the *value* of gold since the 1890's and not the increase in the

[27]See Federal Reserve Bulletin, August 1937, pp. 703–6. Gold in the period of the world economic crisis and the crisis of 1937 is discussed in Michalevksij 1945. As an example of actual dishoarding, Soviet citizens gave up nearly 100 tonnes of gold to Torgsin (hard-currency retail chain) in 1932–35 (Osokina 2009, p. 12).

[28]Which is not to say that private hoarding no longer plays a role. 'The strengthening decay of capitalism in the epoch of its general crisis finds expression in a whole series of phenomena of sharp regression in the field of economics, politics and way of life of the capitalist world. With regard to the function of treasure the regression is manifested in the revival of massive private hoarding of gold' (Michalevksij 1952a, p. 125.). The works on gold by Michalevksij (1876–1952) are informative. His 1937 book studied the question of the value of gold and commodity prices from the beginning of the nineteenth century up to his day.

> *production* of gold, which played a central role in the rise in the cost of living in the 'heyday' of imperialism from 1893-1914.[29]

Let us imagine how Kautsky would respond to this. Gold in the bank (or state treasury) is only 'technically' hoarded. Gold does not literally have to circulate itself to be in circulation. It can be represented by tokens and instructions on it. To be more exact Mandel's (and also Hilferding's) argument should read then, that also the notes received in exchange for gold did not enter circulation, instead were all 'hoarded'.[30] A glance at the growth of the quantity of notes in circulation at the time in the United States already seems to undermine this modified version of Mandel's argument. It is true that like gold, the banknote does not forcefully enter circulation.[31] However, if the gold producer is to continue production, he cannot 'hoard' all his earned banknotes, but must pay wages, raw material and so on, with them.

> If we understand Hilferding in such a way that the expansion of gold production does not at all affect the economy, insofar as the producer of it does not bring into circulation gold, nor the received in exchange for it banknote, then this assumption is simply absurd. With the same right could be posed for any similar hypotheses the question of how the value of circulating gold would be determined, if its new production ceased completely. The answer to this question is generally very simple: gold would have ceased to be money, because it would lose its character of freely reproducible commodity.[32]

Again, while it is true that banknotes, in contrast to state paper money, do not forcefully enter circulation, in this case of the gold producer they still are under an economic necessity, an 'automatic certainty', to do so if gold production is not to cease.

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[29]Mandel 1975, pp. 426–7. However, it is possible to take into account the reserve policy of banks, while staying within the framework of the quantity theory. So Keynes argued that the absorption into central bank reserves of the increased gold output in 1900–14 lessened its effect on the price level, than would have otherwise been the case (see Keynes 1923, p. 81).

[30]'Hoards must not be confused with reserve funds of coin, which form a constituent element of the total amount of money always in circulation …' (Marx 1987, p. 370). Money's function of hoarding cannot be fulfilled by state paper money (which forcefully enters circulation) or by banknotes (which are extinguished when unnecessary in circulation). Reserve funds are 'accumulations of money as means of payment' (p. 379).

[31]Gold certificates issued by the Treasury when it bought gold (after 1933) did not enter circulation. They were deposited in the Federal Reserve. In exchange for them the government received newly created Fed banknotes (leaving aside gold sterilisation), and these entered circulation in paying the seller of gold. This makes the gold certificates, already unusual in that they were hundred per cent backed, of this time an even more peculiar form of state paper money.

[32]Bogdanov 1928, pp. 55–6.

Even if the gold producer could 'hoard' all his notes, the reason why the increased gold production of the 1930s was without effect on the price level (Mandel's reference to the lack of a significant increase of total demand) does not have to be sought in the supposed fact that notes were hoarded. Mandel forgets his own finding that 'between the two World Wars ... the average productivity of labour in gold production at best stagnated, and most probably declined slightly'.[33] In contrast, the huge gold output of the 1890s had been accompanied by improvements in production that reduced its value more than that of commodities. Kautsky could just as well have explained the lack of a price rise in the 1930s merely by pointing out, that no improvements in gold extraction had taken place which reduced its value more than that of other commodities.

Mandel's example operates squarely on the plain of the quantity theory: there was no price rise, because the surplus gold was (could be) absorbed, that is, it did not enter circulation. But to this one can reply (assuming unchanged value of gold): 'the whole surplus gold was absorbed by the banks, because prices were not increased. After all, if prices had risen, for circulation would be needed either new banknotes, or additional gold'.[34]

One and a half pence

Ricardo had been criticised for his assumption that 'gold is money only because it circulates as a medium of circulation, ... it is forced to stay in the sphere of circulation, like paper money with forced currency issued by the State (and Ricardo implies this) ... '.[35] For Ricardo the value of gold bullion could diverge from, for example fall below, its own value. Though Hilferding in one place writes that coin cannot fall below the value of its metal content, he believes the reason which prevents his scenario (of a refusal to buy gold) from being implemented by central banks, is that then their existing gold reserves would fall below their

[33]Mandel 1975, p. 423.

[34]Keller 1925, p. 85. This quote from Keller is from a passage where he criticises Varga. Mandel is right that Kautsky traced the effect of reduced gold value through the increased volume or direct demand of gold on commodities in circulation. Yet Mandel later himself made such an analysis (Mandel 1984, pp. 152–6.).

[35]Marx 1987, p. 402. Of course Ricardo acknowledged the withdrawal of gold coins from circulation when an excessive amount of paper is issued. The prohibition to melt coin (and export the gold) was circumvented in practice. For Ricardo, the withdrawn coins are brought to the 'market' as bullion, and the added quantity on this bullion market will lower the (national) value of gold. In this sense gold for Ricardo is still always in circulation. The 'paper' (banknote) currency because still defined as a gold currency (even when inconvertible), then depreciates due to the fallen value of gold. For Ricardo also in this sense gold is still in circulation (and here he is indeed correct, it seems to us). The commodity price-level rises in terms of the fallen value of gold, and it is this type of price increase which matters for Ricardo (1810, pp. 15–6). Gold can still 'circulate' through its 'paper' representative, even though it is withdrawn from circulation as coin.

own value.[36] This seems to entail Ricardo's position that gold bullion can fall below its own value. And for Hilferding certainly the coin's value could rise above the value of its gold bullion. Like Ricardo, Hilferding believes that a change for example in the needs of commodity circulation will cause a ('quantitative') change of the value of his hypothetical currency, since as forced currency (it seems for Hilferding a restricted or paper currency follows the laws of state paper money) it cannot be withdrawn from (or enter) circulation. This change, here comes Hilferding's *non sequitur*, means, that its ('qualitative') value will now be derived from the value of the circulating commodities, and no longer gold's value (even though to an ever smaller quantitative extent), as it still would be for Ricardo. On this point Hilferding differs and even regresses from Ricardo's theory.[37]

When the mint was rushed, people had to wait before their bullion was coined. Meanwhile the value of coin (that is currency in general) could rise above bullion.[38] The Bank of England would pay less gold coin (or paper) for the same amount of gold bullion, a phenomenon similar to a restricted currency. But at a certain point people unavoidably would start making their (still full-valued) coins themselves, so the deviation would stay minimal.[39] Nevertheless, waiting-time at the mint existed even in ordinary quiet periods. This allows the Bank of England's minimum purchasing rate (£3 17s. 9d.) to be set below the fixed mint and convertibility rate (£3 17s. 10.5d.), that is 1.5 pence or 0.1605 per cent lower. A law was introduced to forbid the Bank to go any lower. The longer the waiting time at the mint, the lower the minimum purchasing rate could have gone. So a free coinage gold system ostensibly has some feature of a restricted currency. This waiting time at the mint is one of the reasons why Ricardo defends a paper currency, eliminating coinage all together, and instead argued for conversion of notes into bullion.[40] And importantly, the provision was that all gold offered would continue to be 'bought', that is converted into notes. Ricardo 'declared that paper money is the most perfect form of money'.[41] Of course this would in fact still be defined as a gold currency, even its perfected version. It can be argued that some form of Ricardo's plan was realised for a period in the twentieth century, but his and Hilferding's hypothetical scenario, to which their (different) theories of restricted currency could be applied, were not, at least certainly not before 1971.

[36]See Hilferding 1912a in this volume.
[37]See Berkovsky 1930a, p. 77.
[38]See Mushet 1819, pp. 338–42.
[39]See Ricardo 1811, p. 91.
[40]See Ricardo 1819, p. 28.
[41]Marx 1987, p. 415.

Soviet gold in Switzerland

For gold to be minted, or coins to enter into circulation, we see also in the case of Switzerland after the war that the Swiss franc's exchange rate with the gold dollar (the Swiss gold 'market price') had to fall a bit below the mint price, that is minus minting and waiting cost. Karl Kautsky's son Benedikt in a letter to his father gave it as an example, which he thought illustrated Hilferding's scenario.[42] The notes were inconvertible and the bank refused to convert ('buy') gold into them. To be sure, since coinage was not restricted there, Hilferding's theory could not even apply. It is good to dwell on it nevertheless, because we witness a rare case where individuals made actual use of the right of free coinage. A few months in early 1922 the Swiss exchange rate moved below its dollar parity, that is the franc appreciated. In this period Europeans who normally exported gold to the United States, seem instead to have chosen to mint their gold in Switzerland. Thanks to the exchange rate they could then exchange Swiss francs into dollars without a loss, thus saving them the shipping costs over the Atlantic ocean. Indeed large amounts of gold were entering Switzerland from Sweden, originally Russian gold payments.

> In the last weeks a very interesting phenomenon developed: The dollar sunk below parity against the Swiss franc. ... here by private initiative gold currency is re-established. The particularity of the matter now is that in America there exists no disagio of paper money, so that the Swiss make a profit when they buy gold dollars at parity, exchange them for franc notes and for these buy again gold. The profit with the lowest dollar position (5.11 against 5.18 parity[43]) would consist of more than 1 per cent. An example for Hilferdingians and a proof, how crazy the present world order is, how nevertheless ever again the gold currency sets itself through.

It is difficult to understand where the profit according to Benedikt Kautsky would lie here. Submitting a kilogram gold to the Swiss mint would get an individual 3444 fr gold coins in return, though minus minting- and waiting (20 days, loss of interest) costs it was 3421 fr. When the 'market price' of gold falls below 3421 fr (that is, the exchange rate falls below 5.148), you still continue to get the same 3421 fr by bringing it to the mint. So if for example

[42]Benedikt Kautsky, letter 8 January 1922 to Karl Kautsky.
[43][One kilogram gold = $664,6 = 3444 4/9 fr. (One dollar = 1.50462 gram.) Today currency exchange rates do not have a constant parity.]

at the lowest dollar parity that was briefly reached (the 'market price' for a kilo gold then was 3400 fr) an individual were to export a kilogram gold to America, and exchange dollar notes into franc notes, they would get only 3400 fr. Whereas if they minted the gold in Switzerland they got 21 fr 'extra' (so not actually one per cent). But this is only in comparison to if they had originally intended to export it to America, and had wanted to exchange the received dollar notes back into francs at the now unfavourable rate. That is, instead of converting these dollar notes first into gold coin dollars, and submit the gold dollars to the Swiss mint. So this is an imaginary 'profit' derived from a comparison to an implausible scheme.

A similarly wrong claim made in the press was, that 'the absurd position has arisen that the Swiss bank-note actually commands a higher price than the 20 franc gold piece'.[44] In fact both the note- and gold franc equally were quoted in more dollars, than at the exchange rate's parity. But because free coinage existed in Switzerland, no actual 'command' over more American dollars took place. What would be really absurd is that 1 kilogram in gold francs (or 3444 fr notes) could have commanded for example 1.05 kilogram in gold dollars. In general under a gold system (and as we see in the Swiss case, even under an inconvertible currency but where free coinage continues to exists), there is no such unequal exchange of gold currencies. In this case Americans could always send gold to the Swiss mint. This did not even have to come from over the Atlantic, as Benedikt Kautsky points out: 'Consequently the New York banks no longer pay in bills of exchange, but in gold, which they get from Paris and now redirect to Geneva'. This fits with normal procedure under a gold system when the parity is breached.

In total a worth of 67 million francs was newly coined (19.5 tons). In addition almost double that amount of (evidently privately hoarded) gold coins surfaced into circulation, which means that even if free coinage had been abolished as in Hilferding's scenario, there still would have entered gold into circulation. Gold coins continued to circulate even for months after the exchange rate had moved back (under parity). All gold coins that were brought in for deposit, were again handed out when other clients withdrew a sum from their deposit (and this led some to the wrong belief that the notes had become redeemable[45]), since the central bank refused to increase its gold reserve.

[44] *The Saturday Review*, 7 January 1922.
[45] See Young 1925 (volume 2), p. 287.

Chapter One

Money (1918)[46]

Karl Kautsky

Karl Kautsky (1854-1938), the most outstanding theoretician of the Second International (1889-1914) needs no presentation to our readers (the best biography is Waldenberg 1980). We will only recall that, before becoming the most famous "renegade" of revolutionary Marxism (Lenin 1918), he was widely recognised as the foremost authority on Marxian economics, both as editor of the first edition of Marx's *Theories of Surplus Value* (Marx 1905-1910) and as author of the book *The Agrarian Question*, which Lenin called "the most important event in present-day economic literature since the third volume of *Capital*" (Lenin 1899). Kautsky was also the author of the most famous introduction to Marxist political economy of the period, *The Economic Doctrines of Karl Marx*, originally published in 1887, issued in numerous revised editions and translated to several languages (Kautsky 1925, see the summary of Marx's monetary theory in that book, Part I, Section II: Money). Since *The Economic Doctrines of Karl Marx* is nowadays available online, we have chosen to open our anthology with this selection from chapter seven of Kautsky's *Social-Democratic Remarks on the Transition Economy* (Kautsky 1918). The selected material is a popular exposition of the historical development of the functions of money; by placing this piece at the beginning of our book, we are following the order of the anthology of Marxist essays on the theory of money issued by the Soviet People's Commissariat of Finance (Shmelev et al., 1929).

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'After the winning of state power in Russia by the Bolsheviks in November last year, one had to consider the possibility, though not yet the probability, of the rapid conclusion of a general peace treaty and thus the approach of the transition economy. [...] I finished the present writing therefore already in March, about the time of the Brest-Litovsk peace treaty. [...] I devoted more than a third of the book to the money question. It seemed to offer the most

[46]Kautsky 1918, pp. 105-141.

theoretical difficulties and here one could presuppose the least, since a popular presentation of the money system from the Marxist standpoint is still lacking. It seemed to me therefore necessary, in order to show the foundations of my conception, to offer a generally understandable exposition of the theory of money. […] Precisely about the money system the most outlandish notions hold sway'.

1. The beginnings of money

Until now we have considered the problems of the transition economy mainly from the material side, i.e. the problems which arise from the fact that in the war the material wealth of society suffered a tremendous reduction through the destruction and constriction of production and transport.

As long as these problems are of a purely material nature, they would, assuming the same extension and technique of the war, remain the same in all modes of production.

They obtain, however, in commodity production a peculiar duplication and increased complexity through *money*. Within commodity production any transformation of the material in the production process, from the first appropriation of raw material in nature until the ultimate appropriation of the finished product by consumers, signifies not only a change in location or form, but also a monetary transaction. All the movements and changes in material wealth are thus reflected in the movements and changes of sums of money, though often in a very distorted form. All material questions of economic life now appear simultaneously as questions of money.

Yet money in commodity production is not merely the mirror of the economy, but also a mechanism that is indispensable to keep it running.

Like much else, due to the world war also this peculiar mechanism is now in thorough disarray. he restoration of this mechanism is as important as the restoration of means of transport, of means of labour and objects of labour. We must therefore also consider this question before we conclude our study of the problems of the transition economy.

The monetary system constitutes one the most difficult and complicated mechanisms, since it is often a question merely of mirror images, of abstractions that are not tangible as a ship, a locomotive, an arable field, a factory.

We must therefore, before we approach the money questions of the transition economy, give a brief theoretical introduction about money, wherewith we however will not review all its

aspects – that would lead us too far –, but only those that come into consideration for our immediate purpose here.

The most popular form of developing economic concepts is to offer a presentation of their historical development, and that is the approach we have selected also here. This means that each one of the phenomena we treat is examined in its emergence. But in no way does the sequence in which individual phenomena are discussed always correspond to the sequence in which they arise. This would occasionally complicate rather than facilitate the exposition, since what belongs together would be torn apart. So I will treat, for example, paper money in connection with coin, before we deal with the bill of exchange, although it historically appeared after the bill of exchange.

We proceed from the difference between the original production for the satisfaction of the producers' own needs, without money, and commodity production with money. This difference has already often been stated and can be considered as generally known. So just briefly let it be pointed out, that people for many thousands, probably hundreds of thousands of years lived in small communities, which produced everything their members needed. This mode of production continued even after class differences appeared. The servants and tributaries satisfied the needs of their masters, as well as their own, by direct performance of labour or delivery of products.

The development of the forces of production through the division of labour could not advance much within the framework of primitive small communities. A new way for this development was opened when different societies, which produced different things, came into contact and exchanged different products with each other. Therewith the production of *commodities* was initiated, that is, of goods that were made by the members of a community or an establishment, not in order to consume them themselves, but to exchange them for goods that those people needed but did not produce themselves. With fully developed commodity production everyone produces what he does not need [in order to exchange it for what he needs].

The larger the circle of labourers who work for each other, the more extensively can the division of labour, with its economic benefits, be expanded. The development of commodity exchange made it possible to extend this circle beyond the size and area of the individual community, and to enable the development of the division of labour as far as the area of exchange traffic reached.

This extension however was not so simple. When producers of various commodities came together on a place of exchange, a market, to exchange their commodities, the success of this

operation presupposed that the individual not only found what he sought, but that the owner of the sought-after thing also desired precisely that commodity which the individual had brought into the market.

Let us assume that a carpenter came to the market with his table. He needs linen. The weaver can also be found there, but he already has a table. What he wants is flour, to put a hearty meal on the table for his hungry children. Now enters also a miller with a sack of flour, but he is a thirsty soul. He pushes aside the linen offered to him and asks for wine. Two barrels of wine temptingly stand in front of him. However, the winemaker has set his mind on the purchase of a table, not flour. The table, however, is to be had only against linen.

So none of the exchanges can come about, all commodity owners must return homewards with their products without having achieved anything. It is a rare coincidence that two such exchangers come together, each one of which desires the product of the other.

Indeed the beginning of exchange economy is only possible in such a manner, that each production unit essentially generates everything it needs and only exchanges the leftover or the superfluous, so that its existence does not depend on the conclusion of exchange.

The majority of humanity finds itself already at the beginning of the historical era in this transition state of pure consumption economy to pure commodity production, and it has remained there frequently even among cultured nations, to our very day. In the country villages even today the craftsman practises agriculture, and in backward areas the farmer produces himself most of the manufactured products he needs.

At first exchange would have been something occasional and accidental. Once it started to regularly repeat itself and grow in size, it easily came about that certain commodities were desired more, were taken in exchange easier than others.

Once a commodity had gained that position, it was a logical step that commodity owners who could not exchange their commodity on the market for the one they needed, preferred to exchange their own difficult-to-dispose-of commodity against the more easily exchangeable one, rather than leaving the market without any exchange. They could hope to attain sooner the good which they desired for this easily exchangeable commodity than for their own product.

An example makes this clear. Let us take the above given case of the carpenter, weaver, miller, winemaker, all of whom could not get rid of their commodity. Now another commodity owner appears; the owner of a cow. Cattle has become a commodity which everyone wants and which therefore is soonest taken in exchange.

The owner of the cow takes a look at the different products on the market. He needs a table,

and therefore offers his cow for the table. The carpenter needs no cow; he has three on the pasture. But he knows that the cow is easy to get rid of, so he rather gives the table for it than carrying the table back home.

In possession of the cow, the carpenter turns to the weaver, whose linen he desires. The weaver has no need of the cow or the table, what he wants is flour. But as the miller needs no linen, the weaver accepts the offer of the carpenter, and accepts his cow for fine linen. The carpenter has now sold his table and gotten the desired linen, he disappears from the market. The same transaction by means of the cow now takes place between weaver and miller and finally between miller and winemaker. They now get everything they need, which would have been impossible before. The cow however will change masters until eventually someone is found who really needs it as dairy cattle and keeps it. For the others it merely had the use value of mediating their exchange. This use value is a new use, which does not derive from its natural properties, but from its role in the market. Through this role as general means of exchange it becomes *money*.

Through money, exchange operations are made possible that would otherwise be impossible. Only where money has become common does the sale of commodities receive a rapidity and security that allows the individual to dedicate himself exclusively to the production of his specialty, thereby expanding the division of labour as much as possible.

However, there is also a negative side. Where through the use of money commodity production is fully developed and has taken the place of production for the producers' use, the individual commodity owner completely depends on finding a possessor of money who is ready to buy his commodity. It doesn't matter how much he produced – without money the product does not find the path from producers to consumers.

Money is the most indispensable means of commodity circulation, it wanders from the hands of those who produced the commodities and do not need them into the hands of those who need the commodities and have not produced them.

Simultaneously it develops still another feature. Let us recall the above example prior to the emergence of money. The carpenter wants linen, the weaver flour, the miller wine, and so on. Where it comes to a direct exchange, it is an exchange of dissimilar use values. The dissimilarity of use values is the motive of exchange.

Now money emerges, before the emergence of metal money, let us say in the shape of a cow. All the different use values are now exchanged against one and the same good, which has no use value for any of the exchangers outside the exchange traffic. The cow as money comes into consideration as a new form of value – as *exchange value*. All the different use values

now exchange against the same exchange value – 1 table, 10 meters linen, 50 kilograms flour, 100 litres of wine are each equal to 1 cow. The producers only care about the amounts of each of the different products the cow as money is exchanged against. By indicating these amounts, money becomes the measure of commodity values.

These values are determined by the amounts of labour socially necessary for their production and reproduction. The exchange of equal values is nothing but the exchange of products manufactured with the same labour expenditure.

Already in subsistence economy we find the pursuit, by equal and free producers who work with and for each other, after equality of labour performance and equality of the share of the common product. Of this pursuit, nothing changes when instead of common labour in the common economy there emerges the working-for-each-other in various separated individual economies. It is rather further strengthened because, instead of fellowship, there emerges the strangeness of the producers. Nobody wants to give more labour to others than the others give to him.

The parties involved are certainly unconscious of this pursuit, because they do not work for each other directly, but exchange products with each other. It obtains a peculiar form of expression when, instead of use values exchanging for use values of another kind, the most various use values all come to be measured against the same exchange value.

Whoever now sells his commodity above its labour value, receives in exchange for the product of his labour a product containing more labour, more money, than those who sold their own product at its value or even below it.

This process cannot repeat itself without one accumulating more money than the others. If the commodity producers are free and equal and if commodity production proceeds without inhibiting provisions, then the result will be that the producers will shift to the branch of production where the result of the same labour expenditure delivers more money, than those branches where their labour fetches less money.

The supply of commodities paid above their value will rise and depress their price, while the demand of those paid below their value will decline and thus increase their price. Thus, through the change of supply and demand and the corresponding fluctuation of prices, does the law of value operate.

This holds for simple commodity production, in which the producer who brings the product into the market, and the labourer are the same person. The matter changes somewhat when production is capitalist, i.e. when the producer does not create the products himself but employs paid wage labourers for this. It is no longer the product of his own labour which the

producer now brings into the market, but the product of the labour of others, whose labour power he has bought together with the means of production. He no longer counts the labour expended in production but the money expended, the production costs. He too pursues equality in the yield, like the labourer of simple commodity production; not, however, equality of the yield of labour expenditure, but equality of the yield of money expenditure, that is, the equality of the profit rate.

Thereby the law of value is slightly modified, but in no way cancelled. Now it is not only possible, but even necessary for the market values of some branches of production to stand above their labour value, not merely temporarily, but constantly, though they can do so only to the extent that others constantly stand below it. The mass of labour and thus of labour values over which society disposes is given, and the total mass of the market values must coincide with it. The labour value remains the starting point and the axis around which the whole system of commodity exchange turns. Thereby is given also the mass of surplus value and of profit as well as the level of the profit rate and the deviations of market value from labour value determined by it.

Yet labour value never appears directly. The value of commodities on the market is not measured by the amount of labour that was socially necessary for their production, but by the amount of the money commodity that required the same expenditure of labour. This amount of money is their price.

Just like any result of conscious human activity must be present first in the head of man, as a goal or intention, before it becomes practical reality, so also the value of the commodity must be measured in money, its price set in the head of the producer, before he sells it. The circulation of commodities is impossible without their prior value measurement. This function of money is as indispensable and important for the progress of commodity production, as the circulation itself. Yes, as a means of circulation the money commodity is more dispensable than as measure of value.

The ancient Egyptians for example already used copper and gold (not silver) in the third millennium BCE as money commodity and as the general measure of value of commodities. But the commodities whose value was measured in money were mostly exchanged *in kind* against each other.

So in one of these exchange transactions, for example, a bull was exchanged. Its value was set at 119 copper *utnu* (14.4 kilograms of copper).[47] For it was given in exchange a reed mat

[47]Maspero 1892, p. 20. [“Most of the objects which changed hands at markets were goods for simple everyday requirements; they changed hands mainly by way of barter. For instance, a pair of sandals was offered for a string of beads or for some measures of grain. To a large extent, however, a common denominator was used to

computed at 25 *utnu*, 5 measures of honey at 4 *utnu*, 8 measures of oil at 10 *utnu*, and seven other things for the remainder.

Here copper functioned only as measure of value. It would have functioned as means of circulation if the owner of the bull had been paid 119 copper *utnu* for it and had then bought the mat and the other things with them.

The fact that copper functioned in ancient Egypt more as a measure of value than as a means of circulation probably derived from the fact that copper was wanted too much as a use value. Precisely this fact made it very suitable as money commodity, but it prevented, as long as its production was not very extensive, its utilisation as a means of circulation, because as long as it circulated as such, it was of course not industrially usable.

Even with precious metals, their utilisation as money seems still until the last century to have stood behind their utilisation as object of consumption. Marx cites a calculation of Jacob in 1831, according to which, of the precious metals existing in England a third had the form of money and two-thirds the form of luxury articles.

> [W]hile in Europe as a whole and America, 25 per cent more precious metal was used in luxury goods than in coins.[48]

With the actual money metal of today, gold, new coinage now certainly outweighs industrial application. In 1911 in the world there were

	coins minted	industrially used (estimation)
Gold	372 million dollars	166 million dollars
Silver	117 million ounces	142 million ounces

In discussions of money questions it is usually too little observed, that the material that provides the money finds application not merely as such, but also as a use value and a commodity, i.e. that it appears on the market not only as money, but also as a commodity, and that it can take sometimes one, sometimes the other form without any value alteration. No less frequently, however, the role of money as a measure of value is overlooked, a role that it can only play because as commodity it represents a determined labour value. Money is mostly viewed only as a means of circulation. Thereby it is easy to arrive at entirely wrong

facilitate the barter. This common denominator was the unit of weight of copper, the *uten,* or *utnu,* or *deben,* or *tabnu* (as it is variously called by various writers), and its subdivision the *kit,* or *chat,* or *kedet***.**" Einzig 1966, Chapter 2: Copper Unit of Account in Ancient Egypt, p. 195.]

[48]Marx 1987, p. 369.

conclusions, since money as a measure of value does not at all follow the same laws as it does as a means of circulation.

Both already differ in that money, when it is used as a measure of value, must be present only in the imagination. In contrast, money which mediates a purchase must really be present.

But then again, if money as a measure of value is just imaginary money, this must still be the actual, real money commodity, which cannot be replaced by any other. In contrast, money as a means of circulation, which in exchange must function in its corporeality, can be substituted by surrogates that perform in its place the transfer of money from the hand of the buyer into that of the seller.

The shoemaker can set the price of a pair of boots which he made, for example, at forty marks, without forty marks or even one mark being in his possession or somehow in sight. But he could not set it if the value of gold was not just as fixed as that of the boots, so that the latter can be expressed as a determined amount of gold – as much as two 20 mark coins contain.

For money as a measure of value there are no valueless or undervalued surrogates.

In contrast, it is different with money as a means of circulation.

2. Coin

Which commodities are so often exchanged and sought-after that they eventually attain the function of general means of exchange, of money, depends entirely on the relations of production and exchange of a country. The most various commodities became money: cattle, slaves, furs, salt, cocoa beans, and so on.

In the end, however, it is the precious metals, along with copper, which impose themselves as the money material, thanks to their natural properties.

Already their inalterability makes them suitable to function as money. A commodity is bought to be consumed, to disappear in its acquired form; it falls out of circulation. Money, in contrast, remains within it. It goes from one hand to the other; it is not consumed in anyone but used for a new purchase; it represents for each subsequent seller and buyer the same value as for the previous ones. Cattle and slaves, however, can become sick or even die; fur is threatened by moths; cocoa beans also have no eternal storage life, and so on. Gold and silver, in contrast, remain always the same, and copper is inalterable at least in dry air, which in the primordial places of culture, Egypt and Babylonia, prevailed.

In addition, among the individual pieces [of precious metals and copper] there are no differences in quality and therefore in use value, which often were very significant for the other commodities which functioned as money. The individual pieces are differentiated only by their quantities, that is, by their weight, and are thus particularly suitable for embodying exchange value, which, unlike use value, brings only the quantitative differences of commodity values to light.

In addition, the above-mentioned metals are pretty soft and divisible at will without too much trouble. Through none of these divisions do they lose the use value which they have besides their function as money; they can just as easily be converted from money into commodity as from commodity into money.

Their use value and therewith their commodity value remains with them even when they are divided, to whatever extent. This divisibility is however indispensable, given the large differences in the values that come into the market and circulate there. If I have a gold bar which weighs a pound and I want to buy a commodity whose value is only equal to that of a tenth of the pound of gold, it poses no difficulty to take out of the clump of gold a piece that makes up one-tenth of its weight. But how to cede a tenth of an ox, or of a slave, or even of a fur?

Another factor that favours the utilisation of precious metals as money is their easy transportability. They are of high value and were formerly even more so than now. An immense amount of labour goes into a small weight of precious metal. In a few pounds and in a small space one could transport, with gold and silver pieces, large sums of value. One had no reason to fear that they would suffer during transportation. This made the precious metals particularly suitable for the purposes of commodity trade, which was international from its beginnings and already early on connected wide stretches of land together.

To all of this is added finally the circumstance that the value of the precious metals changes only slightly and slowly. To be sure, the value of every commodity is not determined by the labour time actually spent on its fabrication, but by the socially necessary labour time that would be required at the time of its respective value estimation. If the production of a commodity costs one day of labour time and an invention makes it possible to produce it in half a day, the value of the piece produced before that will be reduced by half when it first comes into the market, after this invention has become common.

The influence of changes in the conditions of production on the value, however, does not always become apparent at the same speed. It will most quickly assert itself in those commodities that are consumed most rapidly, of which no large stocks can be stored for

years and of which the majority must therefore be produced again and again—for example, with cereals. Their value fluctuates considerably depending on the outcome of the harvest, which makes the same amount of agricultural labour be incorporated sometimes in a large and sometimes in a small amount of cereals.

The greater the mass of stocks, the smaller the addition of new commodities delivered by new production, and all the more slowly will changes in the conditions of production change the market value.

Due to their high degree of indestructibility, however, the old stock of precious metals is so large vis-à-vis their new production as in the case of very few other products. Their annual destruction by chemical processes and abrasion is very slight; particularly since objects made of precious metals are usually treated with extreme care, due to their high value. Wilhelm Lexis calculated the annual wear of gold at about 0.2% of the stock. The total amount of existing gold for the year 1900 he calculated at 35.5 billion marks;[49] the annual production of that year covered 1 billion marks, that is, even not 3 per cent of the stock. Since then, the stock increased to more than 50 billion and annual production to almost 2 billion, that is, to 4 per cent of the stock. For the year 1550, Lexis estimates the gold stock at 1700 million, with an annual production of around 20 million, that is, a little over 1 per cent of the stock. Thus, despite the enormous growth of the gold stock, the relative growth of annual new production has increased. The amounts of gold that flowed to Europe were however, in the sixteenth and seventeenth centuries, far in excess of the sum of new production, since at once great masses of gold that had been piled up in America and India for thousands of years were robbed by Europeans and dragged to their homeland.

The major changes in the conditions of gold production which the statistics of new production show us, did not of course remain without influence on the value of gold. Gold value has dropped tremendously since the sixteenth century. Anyway we may assume, with the relatively low growth which the gold stock annually experiences through new production, that even now changes in the production conditions of gold make themselves felt less rapidly in market value than with other commodities, and that this held true to an ever higher extent in earlier centuries.

The market value of the precious metals is less subject to rapid annual fluctuations than, for instance, that of cereals. Then again the average value of cereals has fallen less since the Middle Ages than that of precious metals. The productivity of labour in agriculture did not increase as rapidly as in mining.

[49][One mark equals 0.35842 g of gold.]

So already Adam Smith observed that the value of cereals fluctuates from year to year more than that of gold and silver, but that in the course of centuries it changes less:

> But the value of silver, though it sometimes varies greatly from century to century, seldom varies much from year to year, but frequently continues the same, or very nearly the same, for half a century or a century together.[50]
> The price of those metals (gold and silver), indeed, is not altogether exempted from variation, but the changes to which it is liable are generally slow, gradual and uniform. … But to make any sudden change in the price of gold and silver, so as to raise or lower at once, sensibly and remarkably, the money price of all other commodities, requires such a revolution in commerce as that occasioned by the discovery of America.[51]

So gold and silver come nearest to the economists' ideal of a money commodity invariable in value as the measure of value, which commodity exchange would require for its smooth running just as much as unchangeable scales, yardsticks and capacity measures. About this Smith says:

> But as a measure of quantity, such as the natural foot, fathom, or handful, which is continually varying in its own quantity, can never be an accurate measure of the quantity of other things; so a commodity which is itself continually varying in its own value, can never be an accurate measure of the value of other commodities.[52]

In addition to its function as a measure of value there arise, in the course of economic development, still other tasks of money – such as treasure and means of payment – that make the invariability of the value of money desirable. We will get to know these functions later.
Desirable as this invariability would be, it can be achieved with the value of money just as little as with the value of any other commodity. But the precious metals come nearest to this ideal.
This is also one of the many reasons that finally made them the sole money materials.
The amounts of metals were measured by weight, and therefore the values were expressed in money as determined amounts of weight of gold, silver and copper. A purchase therefore was

[50]Smith 1909, p. 42.
[51]Smith 1909, pp. 333–4.
[52]Smith 1909, p. 39.

accompanied by the weighing of the money metal.

This was, for example, the regular practice among ancient Egyptians, when they did not exchange products in kind but rather preferred to use the money metal not only as a measure of value, but also as a means of purchase.

Copper and gold, and later silver, rings were used thereto. Maspero describes the course of events with this purchase as follows:

> [This custom of payment by one of the usual metals is so convenient, and dispenses with so many calculations, that it has been adopted even for the minor transactions of daily life. The butcher, the baker, the corn-chandler, all the small tradesmen prefer exchange for metal, which is of small compass and does not spoil, to exchange for objects, often bulky in size, which are liable to deteriorate if kept too long in the house. A pair of ducks is worth a quarter of an *outnou* in copper ; a fan, a quarter ; a bronze razor is worth a whole *outnou*; a pickaxe, two ; a goat, two; an ox-head, half an *outnou* in silver; a leather bottle of fine wine, three *outnou* of gold. It is true that often the rings or twisted wires which represent the *outnou* and its multiples do not contain the reputed quantity of gold or silver, and are too light.] They are then weighed at every fresh market. The parties interested take advantage of the excuse for quarrelling loudly ; when they have declaimed, for about a quarter of an hour, that the scales are false, that the weight has been badly taken and should be tried over again, they get tired of war, come to an agreement, and go away quite satisfied with each other. The evil is more serious when too intelligent and too unscrupulous individuals falsity the precious metals, and introduce as much copper into the ingots as they can contain without detection. The honest trader who thinks that he receives, let us say, eight *outnou* of fine gold, and upon whom are foisted eight *outnou* of an alloy exactly resembling gold, but which contains only two-thirds of it, then unconsciously loses one-third of his merchandise.
>
> But for this danger of fraud, which every one naturally dreads, exchange for metal would have already superseded barter for miscellaneous objects. It will become the universal custom as soon as some method can be discovered which will free the public from the necessity of continual weighing, and will guarantee the purity of the ingots.[53]

This method appeared when on the market an authority, who had the confidence of buyers

[53]Maspero 1892, pp. 22–3.

and sellers, provided the individual pieces of money metal with his stamp, which testified that those pieces were well weighed and fair and contained exactly a determined amount of metal. Such an authority could for instance be a locally respected merchant. The stamped pieces, which he brought into circulation, were of course readily taken only by those who knew and trusted him. Generally and permanently stamped metal pieces were only taken without verification, when a permanent and generally recognised authority minted and brought them into circulation: *the state*. Its metal pieces were taken all the sooner and preferred to the unstamped ones, which they pushed out of the money function, because the state had the necessary coercive power to severely punish any falsification of these pieces.

Thus emerged *money coins*. They are nothing but determined weights of money metal, whose accuracy and fairness the state guarantees by its stamp.

Many money names still bear the characteristic of this origin with them: pound sterling, lire, *livre*. The word *mark* meant in the Middle Ages both a weight – 1/2 Pound – and the mark, the stamp, which was printed on the metal to authenticate its weight.

Today, of course, most have forgotten that the money name referred to a determined weight of precious metal.

Once the minting of coins become customary, the individual could transform his money metal into means of purchase readily accepted by anyone simply by going with it to the state mint and minting if there into coins.

In addition, the state also minted those amounts of metal into coins that it itself wanted to bring into circulation for buying or for other purposes. Today the coinage for the state outweighs the coinage for private individuals.

The first state coins are apparently those that were minted in Asia Minor in the seventh century BCE, partly by the Lydian kings, partly by the Greek city states.

The coin is the first form of manifestation of money by itself. In it the money metal has no other use value than to serve as means of circulation. Metal ingots can still serve both as commodity and as money; as raw material for industry and as means of circulation. Not so with coin. If one wants to use it as raw material, one should undo the minting labour contained in it, melt it. As a coin it is merely money.

For this purpose it was made by the state and it is taken at the value which the state indicates. Hence the view originated that money is a product of the state, and that it was the state which conferred it its value.

How wrong this is, is already evident from the fact that coin functions as money only in the area of the state which has coined it and vouches for it. Commodity exchange first begins,

however, at the boundaries between the communities; international traffic has always been an important part of the total commodity circulation. In this traffic, however, the coin as such means nothing; there the money metal is even today, as with the ancient Egyptians, taken by its weight, not by its stamp; it is not counted, but weighed. There any illusion that it is the stamp of the state which confers money its value is lost.
However, within the state this illusion grows through a series of new functions which money obtains.

3. Means of payment

We have so far assumed a condition in which the commodities are exchanged directly against money; the purchase is paid in cash, the money functions as a means of purchase.
But it is not necessary for the handover of a commodity to be immediately followed by the handover of money. The buyer maybe does not have the money at hand. He expects it later, but needs the commodity immediately. If the buyer has sufficient confidence from the seller then he can come up with a promise, for instance a written one, in which the handover of the money is assured at a later date. The relation of seller and buyer transforms itself here into that of creditor and debtor.
It can arise from an exceptional momentary plight of the latter, but also from normal conditions of commodity circulation. These appear where between producers and consumers the merchant squeezes in as buyer and seller, which occurs when producer and consumer are widely separated from each other. If the producer, for instance, hands over the commodity in England, it does not reach at once consumers in India. It takes time before the commodity reaches them and is exchanged by them for money, which then has to make the long journey back to the producer. If the journey back and forth takes three months and a merchant mediates the transaction, he will often be able to do it only on condition that the English producer, who sells him the commodities to transport them to India and to sell them there, demands the money only after three months. The money functions here not as a means of purchase, which has already been completed without it, but as a means of payment of a debt.
The more commodity production develops and becomes common, a process which becomes generalised only under capitalist production, the more often does money function as means of payment, for example to pay rent or lease buildings or pieces of land. Also in the case of

wages it functions mostly as a means of payment. Here usually the commodity, the labour power of the wage labourer, is not only bought but also consumed, through its labour performance, before it is paid.

At first glance the function of money as a means of payment is not significantly different from its function as a means of purchase. The money for the commodity must still be given, only in one case it happens later, in the other earlier.

But this period can contain a lot in itself. The debtor can go bankrupt or be a scammer, who runs off.

Yet even if everything plays out normally, the future payment has a different character than the purchase with immediate cash payment.

In that situation both parties are free—of course not free from economic needs but from external coercion. The shoemaker who buys leather may desperately need it to prolong his existence. But no one forces him to buy it today and not tomorrow, to buy it from this dealer and not from another, to take this quality and not another, to agree with every set price.

It is different with the future payment. Now in each of these relations coercion has taken the place of freedom: the buyer now must deliver a certain sum of money at a certain date to a specific person for a specific commodity, which he has bought and must keep whether it suits him or not.

This economic exigency provides the coercive power of the state with ample occasions to intervene, regulatively or punitively. And therewith it also gains new influence on the monetary system.

With the coin, the state at first takes over only the guarantee of its weight and its money metal content. It is entirely up to the buyers and sellers to decide whether they take the coin as means of purchase or want to use another means of exchange in its place. With the use of money, in contrast, there is an exigency. This is exploited by the state to enforce the utilisation of its coins in its area as means of payment. Only money recognised by the state is legally valid [*rechtsgültig*]; the creditor is obliged to pay in this money; the debtor is obliged to accept the payment in this money.

This becomes a new ground for support of the illusion that the origin of money and its value rests in state power.

4. Token coin

The illusion that the state can make money and determine its value at will increases further, once it exploits its monopoly of the manufacture of coins, and its authority to force them onto its citizens as legal means of payment, in order to issue money that contains far less real value than it indicates.

We disregard here the many cases in which the rulers committed direct fraud, coin forgery, to fill their purse at the expense of their subjects, to exchange the values created by them against less value. We treat here only of methods that are carried out openly and occasionally are even of economic advantage to the country, indeed may become a necessity.

It lies already from the outset in the nature of the coin, that its real metal value does not match the value which it represents according to its stamp. It is full-fledged at the moment in which it leaves the mint. Therewith begins, however, also its wear and tear. This does not matter though. One does not weigh the coin in order to check its weight, but takes it for what it indicates to be, and indeed was at the moment of its coinage. Of course, this holds only within the boundaries of the state. In international traffic, the money metal is weighed, and worn-out coins therefore hold less precious metals and have less value than newly-minted ones.

Not all coins wear off in equal degree. Some lie tranquil in a cashbox and do not abrade, while others change hands hundreds of times a day, are transported and shaken and lose therewith, through attrition, much of their corporality. In the internal traffic of the state, however, the former are worth as much as the latter.

That is also true of coins of different metals, which are in a fixed relation to each other.

In the beginnings of commodity production, it was not always one commodity, but sometimes several, which side by side functioned as money, both as a measure of value and as a means of circulation and payment. But with developed commodity production, it is always just one commodity which serves as a measure of value, in which the value of all the other commodities is measured. If several metals serve next to each other as money, then just one of them is the real measure of value.

This holds true also for coins. Let us assume, for simplicity's sake (which admittedly is not true for primitive conditions), that the metric weight prevails. Then it would stand to reason, when the three money metals coexist in equal importance, that each is divided into equal amounts of weight; that, for instance, the unit of the gold coin contains 10 grams of gold, that of the silver coin 10 grams of silver, that of the copper coin 10 grams of copper. But it does not happen like that. It is always one metal which gains dominion over the others. One would therefore, when gold is this money metal, choose the weight of the silver coin and the copper

coin so that it corresponds to a fraction of the gold coin. Thus, if the decimal system prevails, the silver coin is made so heavy that it is worth 1 gram of gold, and the copper coin 1/10 grams of gold.

If the value relation between gold and silver is for instance 1: 13.5, then the silver coin will not be minted at 10 grams, but at a weight of 13.5 grams. And if the value relation between gold and copper is 1: 210.0, then the copper coin will have a weight of 21 grams.

Of course also silver could be the measure of value, and the piece of gold could be coined as a multiple of the silver piece, so that its value represents, for example, ten times the latter, hence a piece of gold would be worth as much as ten silver pieces. If the silver piece weighs 10 grams, then the gold piece minted will have a weight of 7.3 grams. Today's German 20 mark coin contains just short of 8 grams of gold.

Gold, silver and copper pieces under this provision stand to each other in a steadfast relation. If gold has become the value measuring metal, then silver and copper coins can now be considered as determined weights of gold, as well as determined weights of their own metal. Herewith a division of labour occurs between the different types of coins. The larger the value which they represent at the same weight, the more suitable they are for the larger purchases and payments as well as for long-distance traffic. The lower their value, the more they are suitable merely for small purchases and payments and for local traffic. For coins employed in the smallest purchases one can generally use only the least valuable metal. It would be impossible to mint into a coin the tiny gold grain whose value is equal to that of one copper penny.

Depending on the rapidity with which they change hands, the coins abrade at an uneven rate, therewith however a difference emerges between those metals which serve as money not only in internal but also in international traffic and those which, because of their great weight in relation to their value, remain confined to local traffic.

With international money metals, the wear and tear of coins means a loss for those who must use them to make payments abroad. Whether they send them out in their coin form or melted in bullion, they are accepted abroad only according to their real weight, not according to their weight as defined by the state stamp. Where the state power in the monetary system wants to serve the interests of trade traffic and not a fraudulent fiscal policy, it hence determines that the abrasion of the coin circulating in the country and containing the metal used in international traffic may not exceed a certain, low amount. Too light coins are drawn out of circulation by the state treasury and melted down.

> According to English law, for instance, a sovereign (Pound piece) which has lost more than 0.747 grain of weight (not quite 0.04 grams) is no longer legal tender.[54]

It is quite different with coins of those metals that are not suitable for international traffic. Their abrasion can go on to whatever extent; they will always be accepted in the country for as much as they represent according to the imprinted stamp. This stamp loses with them any relation to the weight. Such coins can permanently indicate more value than they contain; the state power determines their value.

Once one had recognised this, it was a logical step to mint the coins that were intended merely for local, small traffic, from the outset below value. Coins of this type are called *token coins*. Their occurrence seems to set in first in the sixteenth century.

For them, of course, there is no free coinage for private persons. Where would things end up, if anyone with a pound of silver or copper could thereof have coins minted, for which he could buy two or three pounds of silver or copper or commodities of corresponding value! That would make a fine mess of money. No, this good business the state reserves to itself and it can do it only without injury to the production and exchange process if it carries out the minting of coins within narrow limits, only minting as much as the local small traffic can absorb and needs.

5. Paper money

Once the state began to mint coins that contained far less value than they indicated, a further step suggested itself: to increase the profits which the state made therewith still further by issuing, instead of below-value coins, a practically valueless money paper which contained only an infinitesimal amount of labour, and to replace also the valuable coins by mere money tokens [or signs].

This step was taken when the state went over to the issuing of *paper money*, which began in the seventeenth century, and played a major role in the eighteenth and repeatedly in the nineteenth century. The rulers stopped bothering with alchemy, with gold creation, precisely at the time when they discovered the art of making money out of paper.

The paper money that we are dealing with here is not to be confused with the banknote, which does not follow the same laws. That should be constantly borne in mind when reading

[54]Marx 1987, p. 346.

the following remarks. We are dealing here not about a paper that represents a payment order [*Anweisung*] on available metal money, but about paper notes [*Papierzettel*: slips] that the state issues instead of metal money, which it does not have. They apparently are a creation of value out of nothing.

One might ask how the value of paper money and also of token coins is compatible with the Marxist theory of value, according to which value can be created only through labour.

To this objection must first of all be answered, that the value relation of commodities to each other is not modified in any way when, instead of money metal, paper money steps forth.

The value of paper money is admittedly not determined by the labour which it really contains, but nevertheless it is determined by socially necessary labour time, namely by the amount of labour that would be socially necessary to produce that amount of gold (which we henceforth consider the only money metal) which is replaced in commodity circulation by paper money.

Something similar takes place also in commodity production with the formation of ground rent. The value of the product of the most fertile soil or most productive mine is not measured by the actual labour contained in it, but by the labour that is spent on the generation of the product of the most barren soil or of the least productive mine.

As long as gold is necessary as money and cannot be fully replaced, the value of paper money will be determined by gold. Gold can be replaced as means of circulation only within the state, through state-issued paper money, but not in international trade.

The value of paper money is thus not created arbitrarily by the state but depends on the value of gold that, were there no paper money, would have to circulate in its place. And the state cannot arbitrarily produce any amount of value in this way with slight labour expenditure, but only as much as needed by the internal circulation.

In circulation there is, at a given moment, a mass of commodities with a given value. If they were all sold at the same time, gold would have to be present to the amount of their value, to buy them all. Yet not all sales take place simultaneously, but rather one after the other. Whoever has sold can immediately buy again, so that a coin changes hands many times a day. Let us suppose that in a market commodities arrive with a total value of a 100 million marks. If sales and purchases follow each other so rapidly that each money piece effectuates 10 purchases a day on average, then money pieces for a total value of 10 million marks will be needed in order to enable the commodities to circulate. If there is too little money, then the circulation will not take place smoothly, but occasionally falter. If there is too much money, then a part will remain unused. It is just like with the railways, where the amount of freight-

wagons that are required depends on the quantity of goods to be transported and the speed of their conveyance.

The amount of money pieces required in a country for its internal circulation is thus, under given conditions, of a given size, and likewise the sum of their value. If now in place of such gold pieces one issues paper notes bearing the same value designation as them, then these paper notes will be taken in circulation at the same value as the gold, as long as the total amount of their nominal value does not exceed the value of real gold which they replace in circulation.

The complete opposite occurs when more paper notes are issued than corresponds to the circulation needs. Whatever their nominal value may be, their real total value is determined by the total value of the gold that would be required for the circulation of the commodities without them.

Let us suppose that in a country one billion marks in gold are necessary to keep the circulation process running. The state power replaces, in order to procure itself cheap money, the billion in gold money by two billions in paper money. Then the two billions of paper money will represent no more value than the one billion in gold money which they replace. That is, now 40 marks will be needed in paper money to buy a commodity which otherwise would have cost 20 marks in gold money. The market value of a single money note [*Geldscheines*] sinks, while general level of prices, measured in paper money, rise. It now becomes clear that the state cannot create value in the form of paper money at will, but remains dependent on the law of value.

Now it is in and by itself a matter of indifference, whether the value of paper money is higher or lower, whether the same value carries the denomination of 10 marks or 20 marks, or whether the same denomination indicates a greater or lesser weight of gold. Everything which formerly cost one mark will now cost two marks; I lose nothing therewith, if my income instead of 2000 marks now constitutes 4000 marks.

Not the higher or lower *level* of the money value is important, but its *movement*. Not all commodities follow the value changes of money with equal rapidity, and not all payment obligations adjust to them with equal rapidity. There are classes interested in the fall and others interested in the rise of money value.

A commodity producer who has contracted debts in high-value money and repays them in inferior money wins thereby, if his own commodities have risen in price at the same time. The creditor, by contrast, loses, since he must now pay more dearly for all the commodities which he buys, while his returns from the loaned money remain the same. With short-term

debt this does not play a great role, but it does with long-term debt. For industrialists and merchants this factor is therefore less important than for landowners with mortgage debts. The farmers have therefore always been in favour of money depreciation as a means to reduce the real value of their mortgage rates and debts, if the latter stayed at the same in nominal value.

More important for the working class is the fact that the price of labour power, the money wage, follows the fall in money value less rapidly, and therefore increases more slowly, than the other commodities.

It is a certain fact, which will be further explained in what follows, that the production of the commodity labour power, unlike that of other commodities, cannot be restricted if its payment becomes inadequate. For the commodity labour power is one with the person of the worker, he must reproduce it if he wants to live. And its preservation beyond his own life, the generation and raising of his children, he also does not operate as a business. He does not raise his children, in order to sell them with a gain. Admittedly, under certain circumstances, the sinking of the real price of labour power measured by the price of consumer goods, the real wage, does not remain without effects on its reproduction. Increased mortality and a drop in births can reduce it considerably. But this can first influence the labour market only after a delay of fifteen to twenty years, and therefore does not have the slightest influence on the current supply of labour power.

A period of declining money value was therefore hitherto also always a time of declining real wages. Money wages could increase, but they did not grow as fast as the price of foodstuffs.

In this respect, all the exploiters of the workers' labour power have an interest in money depreciation. But only those capitalists who confine themselves entirely to the internal market, and are fully independent of the world market, profit from this.

In the world market one must pay with gold, as before the introduction of paper money. Since now each country with developed commodity production stands in connection with the outside world, buying and selling commodities to it, there develop within the country with paper money two kinds of prices; gold and paper prices. The latter are in effect in internal trade, the former in foreign trade. These two types of prices stand in no steadfast relation to each other. The value of gold practically does not vary in short periods. That of paper money, on the contrary, varies continuously, as soon as it is issues beyond the limits of the requirements of circulation, so that the value of each paper note is no longer determined by the amount of gold which it allegedly represents. Its value now fluctuates even if no new amounts of paper money are thrown into the market to further reduce the market value of

that money. Paper money, after all, has no intrinsic value; the value of its total amount is determined by the amount of commodity values which circulate and by the velocity of money circulation, by the 'socially necessary circulation value', as Hilferding puts it.[55]

This value constantly changes, because both the amount of commodity values as well as the velocity of money circulation continuously change, and the circulation process of the commodity world sporadically expands and contracts.

Hence the relation between the market value of gold and that of paper money is subject to constant changes, which often come to happen very unexpectedly. Someone who in a country with a paper money economy does business abroad, such as buying raw materials from it or selling articles to it, never knows what the money will be worth which he later will have either to give or to receive as payment. And just as little does someone who begins production of a commodity with foreign raw materials, or of a commodity intended for abroad, know what the relation of paper money to gold will be at the time of its completion. Every projection loses a firm basis, and business prospects becomes increasingly unreliable.

This is the ground on which speculation develops. Commodity production is established from the outset on speculation, even when it seeks to meet real needs. Commodity production is, after all, not planned on the basis of the available productive forces and the needs of consumers, but by independent private persons, each of which must guess the needs of the consumers, the amount of products which they will have to give in exchange, i.e. their purchasing power, and finally the level of the productive forces of his industrial branch, i.e. the expected competition. He has to speculate how these factors will turn out, and act according to this speculation. The more correctly he speculates, the more profitable his business will be.

Every industrialist, every merchant must speculate in this manner. The greater the volume of commodity production, the more a kind of division of labour develops, in this as in so many other areas, in the sense that a type of people emerges who make speculation their special and exclusive business; who intervene in the circulation of commodities, not to produce commodities, or to buy them for their own use, or to direct commodities from producers to consumers, but merely to speculate on the rise or fall in prices, in which they will have all the more success, the more they outshine the average businessman in insight in the circulation process or in economic power to influence it.

The propensity for this kind of business grows all the more, the greater the opaqueness of the market, the more frequent its surprises, the larger and more sudden the fluctuations in

[55][Hilferding 1981, p. 47. Kautsky here seems to adopt Hilferding's position, which before the war he had termed 'Marxist suicide'.]

prices. The more the speculator stands to lose–insofar as he owns assets and does not speculates with someone else's money–, the more, however, he also stands to win. The size of the profits allures the peculator and makes him forget the size of the potential losses, like with any lottery. Careful, reliable business increasingly becomes to be a daring game of chance.

Constant uncertainty and unrest on the market, speculation and swindle, rapid generation of great fortunes and disastrous bankruptcies, general economic disruption—that is the picture that emerges when paper money is issued in excess. And in excess it has hitherto almost always been issued, because it was mainly seen as a means to rescue the state from financial distress.

But we must emphasise here again, that paper money of this kind is not to be confused with the banknote, which admittedly is also a paper note that functions as money, so that it is outwardly the same as paper money. But this slip of paper does not mean a replacement for non-available gold, but an instruction payment on gold, which is actually present. It is not issued by the state, but by a bank; it has its origin not in the prerogative of the state, which is exclusively authorised to it, to coin money, but in the development of the banking system. This we still want to examine, before we come to investigate what consequences result from the nature of money presented here for the transition economy.

6. The banknote

We were able to compare money as means of commodity circulation to a railway, which needs a certain amount of wagons to be able to transport a given amount of goods at a given speed. But not all wagons are always in motion. Sometimes more are needed, sometimes less; therefore a certain reserve must be present, because inevitably, at certain moments, a number of wagons stands still at the various stations.

It is equally inevitable for those who find themselves in the realm of commodity circulation not to put the money that flows to them immediately back into circulation through new purchases, but to let part of the money lie dormant for a shorter or longer period of time, to pile it up, to 'accumulate' it, to build thereof a treasure.

In the beginnings of commodity production such a piling up is the result of mere greed for money. No doubt only commodities constitute real use values and therewith material wealth. The only use value of money, by contrast, is to circulate commodities. Its use value outside

this circulation is null; it can never be consumed, and roves around forever only in the realm of circulation. The labour required to generate money does not therefore increase the amount of use values in society, but constitutes a deduction from this amount. The less metal money society needs, the more use values it can produce. This, incidentally, is one of the useful sides of paper money.

But this is only true for society as a whole. In commodity production, however, everybody produces what he does not need. His commodities are thus of no use value for him. Gold as money, by contrast, is the commodity that everyone takes, and by means of which one can buy every use value that one desires. Gold means accessibility to the use values of society. So the individual is all the richer, the greater the amount of gold he has. Hence the greed after gold and the piling up of treasures.

The greater the amount of gold, the sooner one can however also buy great quantities of consumer goods, or remunerate and mobilize great masses of people.

In addition to the private persons, therefore, also the holders of state power began, already early on, to collect great treasures of gold and silver, as a means of faster mobilisation in war. The emerging capitalism later counteracts this urge for gold or silver treasures. The Prussian kings were among the last to accumulate a war chest in shining coin. Already in 1776 this appeared striking to Adam Smith. In his *Wealth of Nations* he remarks:

> In the present times, if you except the king of Prussia, to accumulate treasure seems to be no part of the policy of European princes.[56]

This Prussian exception admittedly has not only remained to this day, but was even taken over by the new German Empire, which in 1871 founded an imperial war treasure of 120 million marks, which was stored at the Julius tower of Spandau.

In general the pursuit to build up metal treasures fades with the development of capitalism, the art of employing money so that it returns to its owner with a profit. Now the watchword is no longer to accumulate gold, pile it up, to keep it together as dead heaps, but to throw the collected gold back into circulation, to recover it with a profit and in that way to multiply its magnitude, its accumulation.

But if developed capitalism frowns upon treasure building, it develops again conditions which occasionally leave treasure building no longer at the discretion of the individuals, but turn it into an economic necessity.

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[56]Smith 1909, p. 339.

Already the development of money as means of payment works towards this. At some dates larger payments are due, which require a longer saving time. Whoever has to pay his house rent in quarterly intervals, must accumulate money the whole quarter year round, in order to finally have the required sum at the given date. If a manufacturer buys a machine that costs, say, 10,000 marks and wears out in ten years, then he must save every year 1,000 marks, in order to be able to renew the machine after ten years with the collected treasure of 10,000 marks. Even workers must in this way gather 'treasures', for instance in order to buy new clothes at certain intervals.

On other hand, with the sale of the harvest the farmer receives a large sum of money which he does not immediately spend but lets lie partly as treasure, in order to spend it gradually over the course of the year.

Each individual participating in commodity circulation is thus subject to the necessity of building up treasures for certain purposes. The division of labour which characterises commodity production also leads, however, to the function of piling up treasures being carried out by single individuals as a particular business. Whoever holds a great treasure which he does not need himself can help out others who need a treasure and do not have one, for instance a farmer whose house burnt down and needs money to build a new one, or a tenant whose fields did not provide income due to crop failure and therefore lacks the money to pay his ground rent, or a Junker in love with splendour who spends twice as much as he earns. If the treasure builder does not merely loan his money for goodness' sake, but stipulates in addition to the return of the loan a surplus yield, he then transforms his treasure into capital.

Usury capital is, next to commercial capital, the first form of capital. Talking about capitalism in antiquity, one can only think of these two forms of capital. Industrial capital gains importance only since the era of the discoveries and the treasures which these concentrated in Europe.

As soon as there is a possibility to use money in a capitalist way, the opportunity arises to live by the mere possession of money, without reducing the money treasure and indeed increasing it. The possession and use of money treasures now becomes a business in itself.

In addition to money lending, the exchange of money became early on a source of income for money handlers. Each coin was after all valid only within the state that coined it. When many merchants from various corners of the world came together on a market, they brought with them many coins that had no currency on that market. The money handlers with an excess stockpile of money were able to exchange such coins, which they of course did only for a

profit.

When, on the other hand, someone wanted to move from his own country to a foreign land, he had to exchange his domestic money for foreign money.

The exchanging of money on the exchange bank [*Wechselbank*] became the second function of these money handlers, the bankers, next to the loan business.

The deposit business joined in as a third function. The more property one has, the greater the risk that it may be stolen. This danger was easily the greatest with gold, which is easier to transport than most other commodities, and exchangeable everywhere. The owners of great treasures therefore took care already early on to build particularly firm buildings, where they held their wealth [in safes]. Each banker had to do likewise. It was therefore logical that business friends who did not have such burglar-proof repositories should trust their own money treasures to him for storage. The banker could gladly take this over. All money pieces look alike. The money of his business friends was indistinguishable from that of the bank itself. The bank did not take on the obligation to return the same gold pieces but only the same amount of money as soon as its owner wanted to withdraw it. Until then, the banker might do with it what he wanted; he had as much right to dispose over it as over a sum of money loaned to him. He could use these deposits to expand his money business, to increase his profit. This became so profitable for the banks that they sought to increase the money deposits stored with them. To this end they began to pay interest on these sums of money, of course at a lower rate than the one they charged themselves for the money they lent. The difference constituted their profit.

At the same time, the character of the loans changed. At first they were occasioned by emergencies, which were the result of accidents, business incompetence and frivolity, or of disasters such as wars, which forced the state itself to take loans. They brought the creditor profit, while the plight of the debtor was often increased by them; his ruin was accelerated, and the material wealth of the community itself reduced when the loan supported inefficiency and waste.

But once industrial capitalism arose, loans began to operate differently. The means of production that the capitalist applies are not produced by him but by others, as commodities which the producers do not use themselves. In order for them to be applied as means of production, they must first be purchased by those who can and want to use them as such.

It is thus not enough in the capitalist mode of production for the means of production required for the progress and expansion of production to be produced. Those who can employ them must also have enough money to buy them. The faster the money available to

industrial capitalists increases, the faster they will be able to expand production, provided of course that the material conditions and the labour forces are given.

The industrial capitalists therefore seek to expand as much as possible the money at their disposal, by adding borrowed money to their own money. Certainly they have to pay interest on the loan, but their own profit is greater than that. Their profit consists of the excess of the profit over the interest, which Marx called the profit of enterprise. The loans now become a means to enrich not only the creditor but also the debtor, and to promote the development of the productive forces of the land.

The loan capital available to industrial capitalists is increased above all by the increase of bank deposits.

These grow much more rapidly than the total sum of money in the land, since sums of money that people otherwise piled up at home are increasingly deposited in the banks, to bear interest there. The industrial capitalists themselves grant each other in this way loans through the banks. We have already mentioned the example of a manufacturer who, in order to be able to replace a purchased machine after 10 years, had to set aside 1,000 marks each year. These 1,000 marks he does not let lie in his safe, they are transferred to the bank and are loaned by it to other capitalists until the manufacturer recalls the entire sum.

This certainly presupposes developed capitalist relations. First, however, we want to once again return to the beginnings of the banking system, to the hoarders [*Schatzbildnern*], who built strong rooms and whose friends entrusted them with the storage of their own money treasure.

This happened against a note [*Schein*], by which the banker pledged himself to repay the stored money as soon as it was demanded. If this bill was written out in a manner that it entitled its bearer, whoever it might be, to withdraw without a certain amount of money from the bank further formalities, then that was the beginning of the *banknote*.[57]

If the owner of such a note had to make a payment, he could go to the bank, return the bill, withdraw his money and pay therewith. It could, however, be more convenient for the two parties, the payer as well as the payee, for the one to hand over the note to the other in order to save time, in cases where the sum of the note was about sufficient for the payment. A possible excess or deficit could be settled with smaller coins.

In this way the bank notes served as money. They were easier to transport than large

[57][Kautsky has been criticised for deriving the banknote from the deposit receipt, instead of from the bill of exchange (Berkovsky 1930c). Kautsky does specify that he is talking about the beginnings of the banking system. For the derivation of banknotes (or bankers' acceptances) from the bill of exchange see Hilferding's 1909 article.]

amounts of gold and gold coins, which remained in the basement of the bank, where they were saved from wear and tear.

Once such bank notes were accepted as money, it was a logical step for the bank to issue also notes that represented payment orders [*Anweisungen*] on its own gold treasure. With these notes it could do money business just as well as with the gold they represented. Therewith from the outset the bank tended to issue more notes than were covered by its gold treasure. As long as the excess notes were taken, they meant an expansion of the money capital of the bank, but also an increase of the available money stock of society. In the process they stayed secured against any devaluation, as long as the bank redeemed every note that was presented to it for gold.

This redemption always had to be available, because the bank notes were taken only by people who knew the bank and had confidence in its solidity. Whoever was doing business outside this circle, had to pay with gold as before and, if he possessed banknotes, he had to redeem them for gold. Through experience it gradually became clear how much gold in proportion to the amount of its notes the bank had to always have in order to be able to face all the demands for redemption, or conversely, how many notes the bank could issue in proportion to its gold stock without having to face the impossibility of redeeming them for gold.

The greater the business area of the bank, the wider also the circle in which its notes were accepted, the lower the percentage of notes that were redeemed for gold in a given period. It had to be the lowest with a central bank whose business extended throughout the entire state. And the centralisation of businesses made the fastest progress precisely with the issuing banks.

On the other hand, the greatest mischief could be done by swindling note issues, and the most frightful confusion could be inflicted on the money system, whose regulation the state had taken upon itself. And why would it leave the profit to be derived from issuing money to private persons?

So it happened in most states that the issue of banknotes has become the privilege of a single or a small number of state-licensed central banks, which alone are entitled to issue notes and do business with them. They sometimes have to share their earnings with the state and provide it with loans at no interest or at a very low interest rate. Their management is regulated and monitored by the state, which also determines the maximum of unbacked notes that they are allowed to issue as well as the relative level of the cash treasure that they must have available.

This latter provision is often misunderstood. Not infrequently people assume that the value which the notes represent depends on the level of their gold backing, and that it rises and falls with that backing. Thus Paul Umbreit wrote in the *Korrespondenzblatt* of the General Commission Of Trade Unions in an article called 'Trade union questions on transition economy' (9 February 1918): 'When our gold holdings fall, the value of our money value falls with them'.

Nothing is more erroneous than that assertion. As long as the convertibility of banknotes for gold exists, their value is always equal to the amount of gold which they represent according to their denomination. The gold treasure has only the purpose, to secure this convertibility. It can be very low in a country where one usually pays with banknotes, and gold is used merely for business in the world market.

A fall of the banknotes below the gold value can only occur, if their convertibility in gold is cancelled and everyone is forced to take them as means of payment in lieu of gold. This can only be done by a state decree for the notes of a bank privileged by the state. These notes thereby take on the character of state paper money with forced currency [*Zwangskurs*], of which we spoke in the previous chapter. The value of the banknotes can under such circumstances fall. Whenever this happens, however, it will not be the consequence of a fall of the gold treasure of the bank, but because its note issue surpassed the needs of commodity circulation. The value of the banknotes does not depend on the level of their gold backing, but on the proportion of their amount to the value of the circulating commodities and to the velocity of their circulation.

It is somewhat arduous, when for example Dr Alfred Schwoner from Vienna in the *Neuen Züricher Zeitung* of 25 February 1918, in an article about the financial situation of Austria, explains:

> It is not so much the *level of note circulation* that makes questionable whether in fact the note circulation is extremely high. This level is, according to the report of 7 December 1917, 17.7 billion krone as opposed to 3 billion krone at the start of war. It thus increased by 14.7 billion, of which 13.2 billion can be traced back to the debt of the two states of the monarchy with the Notenbank and 1.5 billion to other circumstances ...
>
> The situation is different with our *gold treasure*. In peacetime the Notenbank had a treasure fully sufficient to cover the notes ... the possession by the bank of effective gold ... decreased during the war from 1,150 to 324 million krone.

To these should be added the demands on other countries, so that the gold holdings of the Austro-Hungarian Bank can be calculated at 900 million.

> Also this indicates only a minimal coverage rate for the immense note circulation. But we do not lose heart because of that. We after all do not belong to the blind worshippers of gold. *Production force is more than gold.*

This last sentence is certainly very beautiful; unfortunately, it is mistaken, because gold is a means of commodity circulation, while the production force, by contrast, is not. The production force cannot substitute gold in this function. Just as little could someone console himself about the lack of railway wagons with the fact that the water forces of the country are not affected thereby. Like Mr Schwoner, we are not blind worshippers of gold, but precisely for that reason we appraise the phenomena of Austrian note circulation quite differently from him. He considers the expansion of the note circulation of less concern than the reduction of gold backing. We are of the opposite opinion.

If the circulation of notes had remained the same, then their value would not have changed, with the same volume and the same velocity of commodity circulation, even if the gold coverage had fallen from 1,200 to 300 million. In contrast, each note issue beyond the requirements of commodity circulation must lower the note value, even if gold coverage is increased accordingly.

There are many people who think that one can extend the note circulation to any extent if only the gold coverage increases simultaneously. Others go even further and equate coverage with a pawn. This is fundamentally wrong. Gold coverage has the task of allowing each note holder who needs gold to exchange notes against gold metal, the actual means of circulation. Only as a payment order on gold does the note circulate.

When I, in contrast take, on a loan and leave a pawn as a payment guarantee, that pawn is not money, but a commodity. I give it up precisely because it is not money and I need money. I pawn it, instead of selling it, either because it is unsaleable at that time, or because I do not want to permanently part with it.

Such a pawn-bill [*Pfandschein*] is an instruction [*Anweisung*: payment order] on a commodity, not on money. People who have no clue about its nature imagine, however, that any instruction on a value could function as money. And because they believe that with increased coverage also the number of banknotes issued can be increased at will, they reach the conclusion that with the growth in the number of pawns the number of banknotes could

increase indefinitely.

Often land was considered such a pawn-object. If the state confiscated land by about a billion in value, then, it was argued, the state could also issue paper money by the same amount and use land as its backing. This idea was the assumption behind the assignats economy of the French revolution. It still today haunts some minds.

So, for example, Mr Adolf Damaschke in *The Day of Homecoming* advocates the creation of 'servicemen-smallholdings'. The question of how the required money is to be procured gives him few worries. One simply pawns the first smallholdings created and issues for that amount Loan Bureau Notes [*Darlehnskassenscheine*].

He says:

> We have taken a very important step during the war. Never before has anyone dared to issue money that was not backed by gold. (Mr Damaschke seems to have never heard of paper money in previous times. K.) Because of the war, however, now many people suffer through no fault of their own, for example the manufacturers who cannot export their commodities, the merchants who have goods in colonies, the owners of foreign securities, and so on. To help them, we have set up loan bureaus [*Darlehnskassen*]. In these bureaus, values like the above-mentioned ones can be pawned in exchange for a Loan Bureau Note. This step has been taken without encountering any serious obstacle. We usually do not know whether our paper money says "Reichsbank-note" or "Loan Bureau Note". Indeed, in the end it does not matter at all. The decisive thing is not the piece of gold that lies in the basement of the Reichsbank, or the pawn in the loan bureau, but the fact that the German empire, with its order, with its taxation power, with its honour, stands up for the certificate.[58]

Throughout this whole exposition of Mr Damaschke, as in those of almost all who now write about money relations, one can see that they don't have the slightest clue about the fact that the amount of money, representing a certain value, is determined and limited by the value of the mass of commodities entering circulation. According to Damaschke, a state in which commodities worth 100 billion are pawned should be able to issue 100 billion in paper money.

Loan Bureau Notes and banknotes that are not convertible are subject to the same economic laws as paper money, of which we spoke in the previous chapter. Convertible banknotes, in

[58]Damaschke 1918, p. 20.

contrast, are essentially different from paper money already in their origin. Paper money derives from the state's financial needs; the banknote from the needs of commodity circulation. It can become a means to accelerate it, to increase the productive forces and raise commodity production to a higher level.

We have already referred to paper money as an invention that within certain limits saves labour, which would otherwise be required for the production of metal money, and therewith frees labour forces that become available for the production of use values. The banknote has the same effect in more rational form.

Paper money and banknotes, however, increase not merely the number of labour forces that create use values, they also allow for a far more rapid increase in the amount of means of circulation than can be produced through gold mining. Therewith a barrier is removed which stood in the way of the rapid development of commodity production, since after all a certain expansion of commodity circulation requires a certain amount of money. The amount of values that enter the circulation process grows not only with the population, i.e. with the amount of labour power; it must increase even with a constant amount of labour power, if production for subsistence rapidly declines and production for sale grows. Only the latter needs money for commodity circulation, not the former.

When commodity production reached the threshold of capitalist production, which alone is able to turn it into a general form of production, its development in the sixteenth and seventeenth centuries was powerfully stimulated by the huge masses of gold and silver that flowed from America to Europe and greatly increased the amount of money in circulation. This stream increasingly shrank during the seventeenth century; in its stead the big issuing banks, which emerged in the eighteenth century, opened up a new flow of money, which moreover had the advantage that it did not, like gold and silver extraction, squander labour power required for the production of use values.

Through the banknote it becomes possible to adjust the amount of circulating money to the fastest, most abrupt increase in the amount of commodities brought for sale.

7. Bill of exchange and cheque

Simultaneously methods arise that create no new cash money, but economise it and save time, accelerating the money traffic and therewith increasing the intensity of commodity production, just like the acceleration in the transportation of commodities. Some of these

methods become particularly important for international commodity circulation. Here the banknote plays no role. And simultaneously with the increasing value sums and the distances of commodity trade grow the insufficiencies and difficulties of payments with gold. Also the volume of international trade tends to grow faster than gold production.

For international trade especially the *bill of exchange* comes into play, for internal money circulation the *cheque*. Both become important due to the settlement of payments which they make possible.

We have already spoken of bank deposits and derived the origin of the banknote from one form of access of the depositary to his deposit. Today the depositary has access to it in a different way, through a payment order [*Zahlungsauftrag*], a *cheque*, which orders the bank to pay from the deposit to a third party. If the third party has a deposit with the same bank, this payment can be done without any cash money, in such a way that in the books of the bank the deposit of the one is reduced by the amount of the cheque and that of the other is increased by it (giro).

The bigger the bank, the wider its business traffic, the more numerous its branches, the more often this occurs. The German Reichsbank is used for giro transactions by most major businesses.

In the year 1910, for the one-billion-mark daily turnover of the Reichsbank only 1/8 billion in actual money was required. Only 500 marks in notes were actually employed in the business turnover of the Reichsbank for every 100,000 marks.[59]

In addition, clearing and settlement organisations develop in which the large businesses, particularly the banks, settle their mutual claims and pay in cash or transfer by giro only the remainder (*saldi* or balances). What expansion this method has gained, can be illustrated by some numbers which we take from the above-cited work of Schulze-Gaevernitz. The turnover of the Reichsbank amounted to

[59]Schulze-Gaevernitz 1915, p. 41.

	1891	1913
	billions	billions
in giro traffic	81,0	379,2
in clearing traffic	17,6	73,6
Together	98,7	452,8
Of which cash payment traffic	24,3	43,4
Cash payment as % of total turnover	24.7 per cent	9.6 per cent

Of a different nature than the cheque is the bill of exchange. It is not a payment order, but a payment promise; either a direct payment promise, the promissory note [*Solowechsel*], in which on party promises to pay to the other a certain sum at a given date, or an indirect payment promise, initiated by a payment order. One party pledges himself to pay to the other, or to a third party, a certain sum at a certain time. This bill of exchange has full validity only when the first party accepts it, that is, recognises by his signature that the demand of the other as valid. Thereby the order becomes a payment promise.

Demands from international commodity trade are usually settled in this way. The German exporters to England receive bills of exchange from the local importers there, and the English exporters to Germany receive bills of exchange from the German importers. The exporters here and there sell their bills of exchange, which are due only later, to banks, either for cash or to increase their deposits. So the bills of exchange both here and there flow to a few central institutions, for whom it is not difficult to settle the mutual obligations between the countries. Also here merely the *saldo* or remainder needs to be settled in cash money, which however must be gold.

And gold remains the basis of the whole immense money building that rises up in this way. Its share in the money mass becomes however progressively smaller, and also the share of banknotes declines in comparison to those money sums which consist merely of payment orders, payment promises, and book-entry payment claims. All of these, however, are money, commodity values converted to the money form which have not yet been reconverted into the form of new commodities.

Even though the share of gold in the total mass of money declines, the existing gold mass in money form still increases absolutely due to the progress of gold production. It remains the measure of value of commodities, and any sum of another type of money is expressed as a gold sum. Imposing as the whole paper edifice looks, it remains under the rule of gold, and

no paper currency can change this. Gold remains also the only secure basis of capitalist business. All other types of money are basically only payment promises for gold, and can only act as money as long as the promises of the originator of this money are considered reliable. If the confidence, credit, disappears, then the whole building trembles and threatens to collapse.

Through the development of credit money, mere promises are turned into good coin. While the money economy becomes ever more sensitive to swindles, it opens ever wider more the gates for it. And the greater the uncertainty, all the more speculation flowers.

8. Fictitious capital

This situation is driven to extremes by the fact that fictitious *money* is joined by fictitious *capital*.

We have seen that money capital seeks employment in the granting of loans in exchange for interest. The interest emerged initially from an extortion, from the exploitation of the plight of the debtor, and its rate therefore depended entirely on the level of that plight.

The situation was posed quite differently once the loan became a means to fertilise industrial production, a means not only for the creditor but also for the debtor to gain surplus value. Competition now brings regularity in the course of business and, both in profit and in interest. Despite the small daily fluctuations, an average interest rate nevertheless develops for solid business.

Simultaneously, it also becomes so common to put any money sum that one does not immediately need in a bank or some other interest-bearing place that in the consciousness of business people interest becomes a natural product of money.

> It becomes as completely the property of money to create value, to yield interest, as it is the property of a pear tree to bear pears.[60]

But once in people's consciousness money capital and interest are inextricably linked, when one expects to find interest wherever there is money capital, then the reversal of this relation suggests itself, and people see money capital wherever a regular interest payment exists. And if a general rate of interest is given, then one sees behind a certain amount of interest also a

[60]Marx 1981, p. 516.

certain amount of money capital.

Thus arises a new form of value and capital, which is not a product of labour but a mere calculation, a form which Marx called fictitious, sometimes also illusory capital. If the right to an interest payment is set on paper, then this paper becomes a security, a commodity that one buys and sells just like other commodities.

Behind fictitious capital can stand real capital which is a product of labour, for instance means of production and money for wage payments, but the value of fictitious capital is not measured according to it.

Let us take a joint-stock company, for instance a factory. The price of the shares is not calculated according to the value of the plant, the raw materials and the available cash, but according to the level of the dividend which they yield. With the establishment of the factory the share capital was equal to the real capital applied in the factory, 10 million, and the price of the shares was in line with their nominal value, say 1,000. If the average interest rate is 5 per cent and the company yields an annual profit of 1 million, i.e. a dividend of 10 per cent, then its shares will rise to 2,000. If it yields annually 1 million in profits and the interest rate declines to 4 per cent, then the price of the shares will reach 2,500.

Behind the paper of a government, bond real capital can stand, when for example it is used for railway construction, but the public bonds have the same value even if the state unproductively squandered the money which it borrowed. Their price fluctuates with the general interest rate.

Not only real, also mere *expected* interest already creates a fictitious capital. Thus an undeveloped piece of land, if it can be used as a building ground, receives a price not by the interest it yields, but by that which neighbouring houses yield and which it could also yield, if it were to be built upon.

With the foundation of every joint-stock company the value of the shares is initially based only on the expected dividends.

This enables and facilitates swindling businesses, but it is also the reason why in no other area prices fluctuate as strongly as with fictitious values, which therefore become the main object of the speculation that becomes concentrated on the stock exchange, the market for all fictitious capital.

On the one hand the monetary and credit mechanism of the production process becomes ever more sensitive. On the other hand simultaneously grow the crashes which it periodically suffers. So it seemed that the capitalist mode of production eventually had to end in chaos, in general economic anarchy, which only socialism could prevent.

However already within capitalism a counteraction set in; less through the formation of cartels, which we ignore in this connection, than through the development of the banks.
We have already seen how the centralisation of capital is most evident in the banks. At the same time they increasingly concentrate all the money not immediately needed and turn it into loan capital, which is employed in industry. The individual capitalist becomes increasingly dependent on his bank and the latter gets increasing insight into his business management.
The bigger the bank, the wider the circle of capitalists which it controls, the greater its insight into the general business situation, the greater its power to intervene in the business management of the capitalists, inhibiting here, promoting there.
Swindles and speculation are by no means excluded because of this. Precisely the banking system provides the greatest means and possibilities for swindlers and speculators. But the great central banks [*Zentralbanken*] get increasingly more power to prevent the swindle and speculation that does not suit them, from which they do not profit and which seems dangerous to their own position of power and to their own business. And the abundance of profit accruing to them from regular business grows so prodigiously, that they gladly forgo risky business of smaller scale. They are interested only in large-scale speculations, of such gigantic nature that they are able to overthrow entire empires. The speculations of the great banks become the most powerful driving forces of imperialism.
In the money traffic of individual capitalist enterprises among themselves, however, the big banks increasingly replace the anarchy of free competition by their own despotism. In this contradiction between growing despotism and growing anarchy the capitalist mode of production now moves.

9. The balance of payments

We have in our discussion of the monetary system apparently gone far from our theme of the transition economy. Yet we always have kept it in mind and highlighted especially those aspects of money that are relevant for it. The longer the groundwork has been laid out, all the more shortly we will be able deal with the consequences that we draw for the transition economy.
When people speak of the regulation of the monetary system in the transition economy, they usually have in mind the prevention of currency depreciation, that is, of the sinking in the

value of the money circulating in the country, which manifests itself in a fall in the exchange rate.

The sinking of the value of money is a phenomenon that is not restricted to Germany, but can be more or less observed in all belligerent powers. We have already discussed in the chapter on paper money the economic damage caused by currency depreciation and also set forth its most important cause, the excessive issue of paper money.

The fall in the exchange rate is also caused by the unfavourable balance of payment. During discussions of the currency question this is usually the only factor taken into consideration, and yet it is not the most important one.

The exchange rate is unfavourable, that is, the market price [*Kurs*] of foreign money is higher than that of the domestic money, if the balance of payments is passive, i.e. if the country has to pay more to other countries than it receives from them. This occurs if, for example, the country imports more commodities than it exports and if this surplus is not offset by claims abroad.

To clarify this, we want to represent the mechanism as simply as possible, without the intervention of banks. Let us take two countries which trade with each other, for instance Russia and Germany. Russia sends 2 billion marks of commodities to Germany, while Germany sends commodities for 1.5 billion rubles, 3 billion marks, to Russia. The Russian exporters receive bills of exchange to the amount of 2 billion marks from Germany; the Russian importers in contrast have to pay 1.5 billion rubles, 3 billion marks to Germany. The simplest means to make such payment is for the Russian importers to buy bills of exchange drawn in Germany. By this purchase the Russian exporters obtain money owed to them by Germany. But the Russian importers look for more bills of exchange in Germany (3 billion), than were drawn there (2 billion). One billion marks of bills of exchange more than is offered will be sought after, and the German bills of exchange, set in marks, will rise in price.

The rise in the exchange rate of foreign bills of exchange, however, cannot exceed a certain point when the convertibility of banknotes against gold exists, when each capitalist is able to give his money the gold-form, which alone is valid abroad. The bill of exchange [drawn] abroad is wanted to spare the expense and effort of sending gold. The higher the exchange rate, all the more logical it is to ship gold instead of buying bills of exchange. Once the exchange rate has reached the point where the shipment of gold becomes more advantageous, its rising stops. This point is called the gold point. It deviates only slightly from the gold value. The exchange rates fluctuate constantly, but in normal times within very insignificant limits.

However, this only holds with convertibility of the banknotes against gold. If there is no gold to be had in a country, then this limit for the rise of the exchange rate towards countries where this convertibility is in place ceases to exit. It can rise to an unlimited height and therewith the prices of imported commodities become ever higher, wherewith one cannot exactly distinguish to what extent that is due to the devaluation of the local paper money, which also increases the price of domestically produced commodities, or to the adverse balance of payment. […]

Chapter Two

Colonial Production of Precious Metals (1905)[61]

Otto Bauer

Otto Bauer (1881–1938) was one of the main thinkers of Austro-Marxism and of the centrist tendency within the Second International whose foremost representative, from 1910 on, was Karl Kautsky (Grunenberg 1970). The term 'Austro-Marxism' is used to describe a group of Viennese intellectuals belonging to the Austrian SDAP (*Sozialdemokratischen Arbeiterpartei*) that included, in addition to Bauer, Karl Renner, Max Adler, Friedrich Adler, and Rudolf Hilferding. In 1907 Bauer published the book for which he is mostly remembered today, *The Question of Nationalities and Social Democracy* (Bauer 2000). In the same year he also founded *Der Kampf*, the theoretical journal of the Austrian Social-Democratic Party, and, from 1907 to 1914, he was party secretary. Following Victor Adler's death in 1918, Bauer became leader of the Austrian Social-Democratic Party. From November 1918 to July 1919, the Austrian Social Democrats formed a coalition government with the Christian-Social Party, with Otto Bauer serving as Minister of Foreign Affairs. When Engelbert Dollfuss installed an authoritarian corporatist dictatorship in 1933, Austrian Social Democracy was repressed. After the Social Democrats' failed attempt at an uprising in February 1934, Otto Bauer was forced into exile. He continued to organise the resistance, first from Brno, Czechoslovakia, and later from Paris. He died in Paris on 4 July 1938, aged 56, just four months after Austria became part of Hitler's Reich (for a recent biography of Bauer see Hanisch 2011). This item is the concluding section of Bauer's article series "Colonial Policy and the Workers" published in *Die neue Zeit*, the theoretical journal of the Social Democratic Party of Germany (*Sozialdemokratische Partei Deutschlands*, SPD) edited by Kautsky. Bauer concludes from his analysis that "inasmuch as colonial policy is a means of increasing precious metal production, it brings about diminished purchasing power with unchanged money wages, i.e. not only a reduction in the proportion of the working class in national wealth, but an absolute reduction of the economic well-being of the proletariat."

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[61]Bauer 1905.

Colonial policy has had from time immemorial, and still has, the task of increasing the wealth of the peoples of Europe in precious metals. Therefore we have to examine the effect of increased precious metal production on the economic well-being of the working class. We assume in the following investigation the domination of *capitalist* gold mining.

In some colonial territory one comes across unknown goldfields. It is not difficult to calculate the profitability of new gold mines. The costs are estimated in money, i.e. in gold, just as the surplus product consists of gold. If the ratio of the surplus product to the costs surpasses the average rate of profit, capitals will flow into gold mining until the last capital spent is unable to obtain more than the average profit in the least profitable mine.

Let us assume, for example, that the average rate of profit is 80 per cent. Also in domestic gold mining the last capital spent, which receives no differential rent – we are abstracting here from the absolute rent – can obtain, with a cost of 100 marks, a surplus product of 30 marks. If now gold mines are discovered in the colony, where with 100 marks in costs 160 marks in gold can be extracted, capital immediately starts to stream into gold mining, where it can obtain those high extra profits. It is not just capital that would otherwise have been used in domestic gold mining that now turns to colonial gold mining. Rather, as long as the rate of profit in the gold mining industry of the colony is higher than in all other branches of production, capitals will flow to it which, without the change in the conditions of production of gold, would have flown into other branches of production. This change in the distribution of social capital certainly has its limits. The more capital turns to colonial gold production, the faster sinks also there the rate of profit of the last capital which yields not ground rent; at first due to the technically-determined falling productivity of the extra capital, but also because the rise of commodity prices (which is, as we shall see, brought about by the changing conditions of gold production through the changed allocation of the productive capital of society) also bring about an increase in the production costs of gold mining. As soon as the last capital, which yields not ground rent, receives no more than the average rate of profit, the influx of capital into gold mining will cease. Meanwhile, as we shall see, the average rate of profit itself will have changed.

What effect does the increase in gold production now have on commodity prices? The discovery of new gold deposits attracted to gold production capitals that would otherwise have been used in other branches of production. The supply of all commodities is thereby reduced; the demand for goods, however, is neither greater nor less than it would have been without discovering new gold mines, because the increasing demand of gold producers for

each individual commodity is correspondingly offset by the lower demand from the totality of commodity producers. But if, with a reduced supply, the demand remained unchanged, commodity prices must rise.

We should fend off at this point the suspicion that we wanted to commit ourselves with this assertion to a new variant on the old quantity theory [of money]. We believe, rather, that we stand on the basis of the Marxian theory of money. According to Marx, the prices of all commodities increase when the value of money – the socially necessary labour time required to produce the unit of weight of gold – decreases. But this formulation can be found at a stage of Marx's analysis which assumes, and necessarily must assume, that commodities are exchanged at their values. When we examine the effects of increased gold production under the complex conditions of capitalist economy, we cannot hold on to that assumption. Here is determinant for the exchange relation between commodities and money no longer simply their value, but their price of production. Since the discovery of new gold mines means a reduction in the cost price of gold, it results in an increase in commodity prices.

But here we encounter a strange problem. Due to the increase in gold production, prices rise in all other branches of production, assuming constant costs of production.[62] This means an increase in the sum of profits, including the mass of surplus value. Is it not contrary to the Marxian theory of value that the mass of surplus value should increase, although in society as a whole neither wages have decreased nor the working day has been extended? Only apparently! As a result of the sinking of the cost price of gold, the same money wages are no longer worth as much as before. As commodity prices have risen, the purchasing power of money has fallen. But while the capitalists are compensated for the decline in the purchasing power of money by the rise of the profit rate, the money wages of the workers remain unchanged, because that fact that capital turns to gold production rather than to other production branches does not change the level of wages. A smaller part of the social labour product therefore falls to the working class; of the working day, a smaller part falls to necessary labour, a greater portion to surplus labour. In the rise of the profit rate as a result of the general rise in prices expresses itself nothing else than the *rising rate of surplus value*.

The literary discussion in recent years makes it impossible to utter these words without reservation. That the increase in gold production increases prices and profits is indeed nothing new, but rather an old truth too often overestimated in its importance. But by basing our assertion on the Marxian theory of value, we gain an accurate *measurement* [*Größenmaβ*] of the effects that we expect from the development of new gold mines. In the

[62]The production costs of the individual branches of production are of course raised by the price rise; if we take however production as a whole, then the costs have remained the same, while the prices have risen.

first-operated gold mines the surplus product represents a much higher rate of profit in relation to the costs than the social average. The inflow of capital into gold mining now brings about an equalisation of profits, that is an equal distribution of the surplus value generated in gold production among all the capitals in society – no matter in which branches of production they are invested. Now the surplus value generated, for instance, in South African gold production is certainly very considerable; but in relation to the huge capitals that are active in the whole European and American economic area, it still appears very small. If someone wanted to explain the large fluctuations in the economy during the last fifteen years from the distribution of that surplus value among those capitals, he would prove nothing else than the theoretical perplexity of the detractors of 'discursive political economy'.

If we therefore reject the incorrect application of the doctrine of the influence of increased gold production on prices and profits, we do not think, because of that, that it is less necessary to determine those effects and their influence on the position of the working class. Inasmuch as colonial policy is a means of increasing precious metal production, it brings about diminished purchasing power with unchanged money wages, i.e. not only - as we have found in the agricultural colonies - a reduction in the proportion of the working class in national wealth, but an absolute reduction of the economic well-being of the proletariat.[63]

We have so far assumed the best case for the workers, namely that the European capital flowing into colonial gold production employs even there European workers, that is that with the capital also the workers migrate into the new land of gold. Where this is not the case, a deterioration of the situation in the labour market of the mother country takes place. The workers of the motherland will be threatened not only by higher commodity prices, but also by reduced labour opportunities.

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[63]Admittedly the increase of the mass of surplus value would have as a result also an accelerated accumulation and hence again raise the demand on the labour market. But therewith also any wage reduction would be able to be justified! Also for the workers a bird in the hand is worth two in the bush. If the economic well-being of the working class has increased even at times of increased gold production, that was due to the progress of unionisation, but also, for example, to the increase in the share of productive capital in the total capital. It had nothing to do with colonial policy. When however the discovery of new gold deposits takes place in a depression period and the flow of unproductive accumulated capital into the sphere of production is accelerated, then it can temporarily raise, along with demand for all other commodities, also the demand for labour forces. But here we are investigating the long-term effects of increased gold production on the well-being of the working class, and we therefore have to abstract from the vicissitudes of the industrial cycle. The discovery of new gold mines signifies for us hence firstly not an increase, but a redistribution of productive capital. We will see later that, even without colonial policy, periods of massive 'standstill' [*Totlegung*] of capital would be followed by years of accelerated accumulation. Compared with the typical picture drawn by us, the great Californian and Australian gold discoveries often bore somewhat modified characteristic traits, but that can only be mentioned here. The '*prospector*' [*Goldsucher*] of the 1850s was neither a capitalist nor a wage worker 'in the categorical sense', rather he was often a former peasant, who did not even belong before immigrating to the circle of commodity production.

Let us illustrate our reasoning by means of a recent example! The discovery of rich gold deposits in South Africa has, as is well-known, turned huge capitals from Europe and America towards gold production; capitals of which otherwise certainly only a very small portion would have been used for the production of gold in Europe and America. Whence came this capital? *Some of* it may have been newly accumulated surplus value, which now poured into gold production rather than turning to any other branch of production. If this is the case, it is clear that the discovery of new gold mines caused nothing but an altered distribution of social capital, a redistribution which raised prices but not wages, therefore reducing the prosperity of the working class. *Another part* of the capital flowing into South African gold production, had the opportunity of productive investment not been available, would indeed probably have temporarily accumulated unproductively, remaining still [*totgelegt geblieben*]. That is the usually observed effect of the discovery of new goldfields: it rouses capital from its sleep and thrusts it into the sphere of production, increasing the demand for goods and with it prices, and therefore increasing the demand for labour power. Whoever believes that, without the development of new gold mines, unproductively accumulated capital would never have reached the sphere of production may be satisfied with this description. But to us it seems certain that capital time and again finds its way into the sphere of production also without the random changes in the conditions of production of gold; that the mechanism of movement of the interest rate, prices and wages does not tolerate a permanent standstill of capital. The capitals unproductively accumulated during the depression of 1890–94 have been again completely absorbed by the productive apparatus of society during the following years of prosperity; the low rate of interest and the low production costs – the necessary consequences of unproductive accumulation – have also again supplied those millions to the sphere of production that today operate in the gold mining industry of South Africa. *We have therefore not compared the situation after the inflow of capital to colonial precious metal production with a situation where this capital would have remained unproductively accumulated, but with a situation where it also operated in the sphere of production, but in other production branches.* The development of new gold mines therefore meant rising commodity prices with unchanged or at least much more slowly rising wages. It harmed the workers even when the capital employed European workers in colonial gold mining. In our case, however, the effect of the change in the allocation of social capital is all the more dangerous, because workers do not migrate with capital to South Africa; capital there rather employs foreign workers, and therefore the European labour market lost absolutely.

As is well-known, the British government has allowed international capital to import coolies to Africa. The yellow slaves are brought from southern China to the Rand, where they are bound to work for three years. The total costs per man - including all transportation charges – are 16½ pounds sterling, that is 9 shillings and 2 pence monthly![64] And the English newspapers still boast at how well the poor filthy coolies who wrest the glistening gold from the African quartz are doing. They have even baths and electric lighting in their barracks! Two trips across the Indian Ocean, food, housing, bathrooms and electric light bulbs - all for 9 marks a month! What a triumph of the methods of relative surplus value! But the low price of the labour power due to the importation of coolies represents an artificial reduction in the production costs of gold. Therefore a lot more capital would have flown to South Africa, if the British government had refused to the international capital that exploits the gold mines the permission to import yellow slaves. By this, however, European workers are hit twice: as buyers of commodities and as sellers of their labour power. Again, we recognize what we have already seen in the plantation colonies: that the exploitation of races standing at a lower level of economic development also harms the European workers. The common interests of the proletarians of all countries therefore have deep roots in the nature of the capitalist mode of production.

[64] *Franfurter Zeitung* of 15 December 1904.

Chapter Three

Money (1910)

Otto Bauer

This is a section from Bauer's 1910 brochure *The Rise in Prices: An Introduction to the Economic Policy of Social Democracy*, part of a series of Marxist analyses of pre-WWII inflation which included Kautsky's 1913 supplement to *Die neue Zeit* called *The Transformations in Gold Production and the Changing Nature of the Rise in Prices* (included in this volume) and Julian Marchlewski, *The High Cost of Living, Commodity Prices and Gold Production* (Karski 1913b). Bauer was also the author of the report on "The High Cost of Living" for the International Socialist Congress to be held in Vienna on 23-29 August 1914, which never took place because World War I broke out three weeks before the congress was due to meet (an English version of the report is available online at the Marxist Internet Archive). Bauer concludes from this analysis that "the reduction in the production costs of gold is one of the causes of inflation."

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Capitalist commodity production is based on the social division of labour. Any enterprise that brings its commodities to market must generate a portion of the goods that society needs in order to meet the needs of its members. But the entrepreneur learns only later, only in the market, if his enterprise has produced commodities that society really needs. Commodities that society does not need find no buyer; if the entrepreneur can sell his commodities and get money for his goods, this proves that in his enterprise goods were produced that society needs, that is, that in his enterprise socially necessary labour was performed. If the owner of commodities can exchange his goods for money in the marketplace, then he learns that the individual labour of the workers active in his enterprise, whom he employed for his individual profit's sake, was at the same time social labour, labour through which a need of society has been satisfied. The owner of the labour product receives confirmation that the individual labour satisfies a social need in the money which he exchanges for the labour product.

There is a social relation between all those who work. Each produces goods that the others need. But this social interdependence between all workers is brought about by a *thing:* by the

money which the owner of the labour product exchanges and for which he then can exchange the labour products of all the other members of society. The transformation of the labour product into money is now the goal of all labour, the conversion of money into other labour products is the way to satisfy our needs. Everyone is out for money, everything depends on money.[65] Money, at first only a means of commodity exchange, represents, as soon as all the goods have turned into commodities, all the wealth of society. 'The servant becomes the master. The mere underling becomes the god of commodities'.[66]

In international trade commodities are paid for with gold. When we import wheat from Russia, cotton from the United States, coal from the German Empire, we must pay for those commodities in gold or bills of exchange, which are instructions on gold. Domestically, to be sure, we [in Austria] do not pay in gold but with banknotes, silver, nickel and bronze coins. But all those methods of payment are set by our currency legislation and our currency policy in a fixed value ratio to gold. A twenty-krone note is worth as much as a gold twenty-krone piece, and the value ratio between the gold twenty-crown piece and the gold twenty-mark piece always depends on how much gold is contained in each of these two coins. The price of every commodity is thus the value ratio of the commodity to gold.

As long as free competition holds, the price of each commodity will depend on its production costs. If it is possible to produce goods with lower costs, then the price of the commodity will also drop in free competition. If the price of the commodity drops, then the seller gets for it less gold. We then say that the commodity has become cheaper.

But also the price of gold depends on its cost of production. If it is possible to extract an ounce of gold at lower cost, then the production price of gold decreases. If the price of gold drops, we get fewer commodities for the gold. We then say that the commodity has become more expensive.[67]

Changes in commodity prices can thus have different causes. Commodity prices may rise, because the production costs of the goods have risen or because the production costs of gold have fallen.

The gold mine owners supply the extracted gold to the mints and banks. They get for it coins or bills of exchange, instructions on gold, with which they first of all defray the costs of

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[65]['*Am Golde hängt, nach Golde drängt nun alles'*. A quote from Gretchen in Goethe's *Faust*: "*Nach Golde drangt, / Am Golde hängt / Doch alles. Ach wir Armen!"* (2801-4).]

[66]Marx 1987, p. 359.

[67]Marx says: 'Gold has neither a *fixed* price *nor any* price at all, when it is a factor in the determination of prices and therefore functions as money of account' (Marx 1987, p. 313). That is, read in context, completely right. But in developed capitalist commodity production, also commodity and gold are not exchanged against each other according at their value, but in proportion to their production prices (cost price and average profit). That is why we are talking here about the price of gold. See Bauer 1905.

production of gold. The excess of the amount of gold produced over the production costs remains theirs. It is all the greater, the lower the production costs. With this surplus they then buy commodities. The gold producers do not increase the stock of commodities, since they produce gold, not commodities; but they increase the demand for commodities. They increase it all the more, the greater the excess of gold production over the costs, thus the lower the costs are. The increased demand for commodities with a constant supply drives up commodity prices. In this way, commodity prices are increased by the fall in the costs of production of gold.

Now there is no doubt that the cost of extraction of gold has fallen considerably in recent years. The British government has eliminated, through the Anglo-Boer War [1899–1902], the last barriers that inhibited the development of South African gold mining. Excellent machines were introduced in the gold mining industry. In order to provide mine owners with cheap labour, Chinese coolies were first brought to South Africa, and later 160,000 Kaffirs were lured into the gold mines. In this way, the cost of extraction of gold was reduced.[68] Now it became possible to operate gold mines, whose operation would not have been profitable enough at higher wages and without the new technical devices. Gold production has therefore increased rapidly.

In Transvaal gold production was as follows:

Year	Pounds Sterling
1904	16,054,809
1905	20,802,074
1906	24,579,997
1907	27,403,738
1908	29,957,610
1909	30,925,788

The reduction in the costs of gold extraction in the South African gold mining industry is probably one of the causes of today's rise of prices. We must now give in exchange for each commodity more money, more gold, because every piece of gold today embodies less social labour than before.

The European workers have concluded with the employers collective agreements, in which it is laid down how many krones, how many marks or franks they receive for one workday. Employers pay the agreed wages in krone and heller. And yet the workers are betrayed at

[68]That this is really the case is proven by the many reports of the London *Economist* about production costs in South African gold mining.

every payment of wages, because the krone, the mark, the franc are no longer today what they once were. They represent less social labour and therefore also have less purchasing power than before. If a twenty-crown piece is worth today less than it was worth ten years ago, we have to receive today more crowns for our labour power in order to receive the same value. Money wages must rise in order for real wages [*Sachlohn*], [that is] wages in values, to remain unchanged. And yet the entrepreneurs complain about the *covetousness* of the workers when our unions demand higher money wages. Unions today have the task of adapting the amount of money wages to the changed value of gold.

It is a well-known fact that a section of the working class finds it hard to maintain its favourable working conditions, if the workers in other locations or branches of industry make do with less favourable working conditions. We see the same phenomenon now on an international scale. The reduction in the production costs of gold is one of the causes of inflation. It has its cause in the fact that extremely cheap labour is available to gold-mining capital. The educated, relatively well-paid Austrian railroad workers see their standard of living deteriorated because the poor, ignorant, dirty Kaffir, who extracts the glistening gold in the mines of South Africa, endures a terrible measure of exploitation. However much Germanic racial pride may struggle against it, it is an undeniable fact that our own standard of living, our whole cultural level depends on the standard of living and the cultural level of the black workers in the gold mines of the Transvaal. This shows the international solidarity of all proletarian interests.[69]

Also the capitalist mode of production is based on social labour. Even though each individual entrepreneur thinks only about his individual profit, the result of their activity is that the many millions of persons who live under the rule of capitalism are, more or less fed, clothed, and housed. But the connection of the individuals into a large society is established by a thing, by gold. So this thing became the master of the world. On its whims, on the vicissitudes of its life now depends the fate of millions of people. Millions now suffer under the present rise of prices, because a series of chance events reduced the production cost of gold. A lifeless thing, lifted by the human hand from the depths of the earth, has become the ruler over humankind.

Humanity can free itself from the domination of a thing only when the individual is no longer connected to the community by a thing. If the work of the individual is no longer individual

[69]The rise in prices depends on the extraction costs of gold, not on the quantity of means of circulation and means of payment. When Hainisch [1909] in his study on the causes of the rise of prices adds up all the gold and banknotes in circulation and wants to explain by the increase of this sum the rise of commodity prices, this method harks back to that quantity theory, about which he himself rightly says that it has been overcome. The circulation of banknotes increases because commodity prices rise, not vice versa.

labour that only finds out whether it has satisfied a need of society through the transformation of the labour product into money, but immediately social labour which is consciously planned and managed by society to ensure that all needs find their satisfaction; if the claim of the individual to the goods he needs is not due to his possession of money but guaranteed by his membership in the society of which he is a member, as a citizen with full rights and obligations; if goods are no longer produced as commodities that need to be sold and bought, but produced by all members of society, stored in the magazines of organised society and allocated from there to all the members of society according to the laws adopted by the totality of the workers themselves, then gold will cease to be the ruler over humankind. It will become a simple thing, like any other; good enough, as Thomas More said, to be used for the production of chamber pots.[70]

[70]["They eat and drink out of vessels of earth, or glass, which make an agreeable appearance though formed of brittle materials: while they make their chamber-pots and close-stools of gold and silver." Thomas More, *Utopia*, Book II: Of the Travelling of the Utopians.]

Chapter Four

Gold Production and the Rise in Prices[71]

(17 November 1911)

Eugen Varga

Eugen (Jenő) Varga (1879-1964), a Marxist economist of Hungarian origins, studied philosophy and economic geography at the University of Budapest. In 1906 he started to write on economic subjects and in 1909 he published his first article in *Die neue Zeit*, the SPD's theoretical journal in which the current item was published. In 1919 Varga became Minister of Finance of the short-lived Hungarian Soviet Republic, after whose fall he fled to Vienna. From there he went in 1920 to the Soviet Union, where he worked for the Communist International. Varga wrote the Economic Reports for the Congresses of the Comintern from 1921 to 1935. He was a member of both the Communist Party of the Soviet Union and of the Communist Party of Hungary. In the years 1922 to 1927 he worked in the department of trade in the Soviet embassy in Berlin. In the 1930s he was Josef Stalin's economic adviser, and survived unmolested the purges of those years, when the Stalinist bureaucracy wiped out the Bolshevik old guard and killed an estimated one million people ("The best estimate that can currently be made of the number of repression deaths in 1937-38 is the range 950,000-1.2 million, i.e. about a million", Ellman 2002, p. 1162). During World War II he advised the Soviet Government in matters of post-war reparations. He attended the Potsdam Conference of 1945 as an expert. By the beginning of the Cold War in 1947, Varga fell out of favour with Stalin due to the publication of this book *The Economic Transformation of Capitalism at the End of the Second World War*, in which he argued that the capitalist system was more inherently stable than had been hitherto believed, but was allowed to keep a minor academic position. After Stalin's death in 1953 he reappeared and in 1954 was awarded the Stalin Prize. But the new rulers of the Kremlin were not interested in Varga's predictions of an economic crisis in the United States, since they pursued a policy of "peaceful coexistence" with imperialism. Varga did not return to his homeland of Hungary, but worked as an economic advisor to Mátyás Rákosi. With the fall of Rákosi due to the Hungarian revolution of 1956, and after the takeover of the government by János Kádár, Varga's advisory activity ended (for a recent biography of Varga see Mommen 2011). In this

[71][Varga 1911b. A similar article in Hungarian (Varga 1911a) included more references, for example Koch 1905.]

article, Varga opposes Otto Bauer's "hypothesis that the current high cost of living may be due to a devaluation of gold" and argues that "*changes in gold production cannot be the cause of inflation*", the reduction in the production costs of gold mining having gone completely to increase differential rent in the gold mining industry. This article gave rise to a debate on the Marxist theory of money in the pages of *Die neue Zeit*, which we reproduce in its entirety for the first time in this volume.

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The rise in prices weighs heavily on all proletarian layers, dashing the achievements of their trade union struggles. The workers of all countries stormily call for a remedy.
The learned advocates of capitalism try to prove that the ruling classes are not to blame for the high cost of living, and seek to shift the blame to other factors.
Two theories in particular serve this purpose: 1. that the rise in prices was caused by the workers' wage increases, 2. *that the rise in prices originates in changes in gold production*.
The first theory is so transparent that it does not require serious refutation. In contrast, the second deserves serious consideration, since it appears to have, in some formulations, a large degree of verisimilitude; indeed it even sounds very Marxist. In *Capital* itself we find no analysis of how changes in gold production would affect price formation, but Marx says:

> We know however that, the values of commodities remaining constant, their prices vary with the value of gold (the material of money), rising in proportion as it falls, and falling in proportion as it rises.[72]

And:

> When money begins to function as a measure of value, when it is used to determine prices, its value is presupposed. If that value falls, the fall first shows itself in a change in the prices of those commodities which are directly exchanged with the precious metals at their source. [73]

But the whole of *Capital* is built on the tacit assumption of a constant value of gold (apart from the chapter on primitive accumulation), so that we cannot immediately draw from it

[72]Marx 1976, p. 213.
[73]Marx 1976, p. 214.

any conclusion about the hypothesis that the current high cost of living may be due to a devaluation of gold. Otto Bauer is of this opinion.[74] *We, on the contrary, believe that we can prove that changes in gold mining can have no influence on inflation.*

For this purpose, we want to treat separately all the versions of this explanation. It comes in two main forms:

1. The quantity of gold produced each year has recently increased dramatically; due to the increase in the quantity [of gold], a larger amount of gold must now be given in exchange for each commodity than before.

2. As a result of the introduction of new machinery in gold mining and the procurement of cheaper labour power, the costs of production of gold have fallen; therefore prices must rise.

The first version is based on the 'quantity theory' [of money]; the second on the labour theory of value, or rather on the theory of production costs.

But the quantity theory, according to which the prices of all commodities depend on the amount of circulating medium in circulation, is only correct for a pure unbacked paper currency or for a restricted silver currency, but not for a gold currency.

Money has, as is well known, in addition to its other functions, the function of serving as means of circulation.

> The weight of gold fixed upon as the standard of prices diverges from the weight which serves as the circulating medium, and the latter thereby ceases to be a real equivalent of the commodities whose prices it realizes. . . . This fact implies the latent possibility of replacing metallic money with tokens made of some other material, i.e. symbols which would perform the function of coins. ... Relatively valueless objects, therefore, such as paper notes, can serve as coins in place of gold.[75]

Tokens, however, can only perform that function [of coins] *only if the issue of paper money is limited to that quantity of symbolically represented gold (or silver) that would really have to circulate*. But if more unbacked paper money is issued than the amount of gold symbolically represented by it that would circulate, it will be devalued in the same proportion as the amount of it exceeding the amount of gold needed to mediate commodity exchange. This happened, for example, [during the French revolution] at the time of the *assignats*. In such cases, of course, general inflation develops! The same happens with a *restricted* silver currency, with the difference that the value (respectively price) of the silver

[74]Bauer 1910.
[75]Marx 1976, pp. 222, 223–4.

coins can never fall below the value (respectively price) of the silver contained in them – though, by contrast, it may very well greatly exceed the value of silver, because it is impossible, due to the restriction, to buy raw silver at the market and let it be coined.[76]

But what is right for inconvertible [*unbedeckte*] paper currency and for restricted silver currency is incorrect for gold. *Gold money not only functions as a measure of value; it is not just a symbol of value, but real value*.[77] A gold coin generally contains as much socially necessary labour as the commodities exchanged for it. *A mere increase in gold production would, therefore, only bring about a reduction in the value of money and thereby cause inflation, if the increase were so great that an absolute surplus of gold developed*, if too large a portion of social labour had been used in the production of gold. But that is by no means the case today: the hunt for gold by the central banks is as intense as it has ever been. Therefore, any explanation of the rise in prices based on the quantity theory is wrong from the start.

But to round our argument off, we will assume for a moment the correctness of the quantity theory and demonstrate that the current rise in prices cannot be explained by the rise in gold production, even on that basis.

The world production of gold during the last ten years was:[78]

	Thousands of Kilograms	Per cent
1900	383	100
1901	393	102
1902	446	117
1903	493	139
1904	523	137
1905	568	148
1906	605	158
1907	621	162
1908	666	174
1909	683	179
1910	685	179

Those who view annual gold production as the basis of price formation are quick to offer this

[76]See Hilferding 1981, p. 37 (chapter 2) passim.
[77]'Gold can serve as a measure of value only because it is itself a product of labour' (Marx 1976, p. 192).
[78]*Statistisches Jahrbuch für das Deutsche Reich*. 32. Jahrgang. Berlin 1911. p. 31.

explanation of the rise of prices: the growth in gold production by 79 per cent was corresponded by a general rise of commodity prices of 79 per cent.

But the comparison of the *annual* increase in gold production with the movement of commodity prices is incorrect even on the basis of the quantity theory itself, because in the settlement of exchange transactions not only the amount of gold newly produced each year is employed, but the total amount of gold, accumulated for centuries, present in the European-American economic area. Thus [if the quantity theory of money were] correctly employed, only the increase in the *total* amount [of gold] might be confronted with the movement of commodity prices.

Reliable estimates put the amount the amount of coined and unminted gold available in the European-American economic area at about 12.3 million kilograms[79] in 1900.

In the years 1901 to 1910, 5.8 million kilograms of gold were newly produced. Now, not the whole newly-produced quantity served to increase the circulating medium. Roughly one-third was used, according to the estimates of the US Mint, Helfferich and Lexis, for industrial purposes. Only about 3.8 million kilograms, representing 32.4 per cent of the amount of gold available in 1910, were therefore used to increase the amount of gold employed in the settlement of exchange transactions.

Accordingly, if the quantity theory were correct, an inflation rate of 30 to 32 per cent would be explainable by the increase in the available amounts of gold, *if the quantity of commodities exchanged had remained the same*.

However, this is an absolutely unreal condition! Although we have no statistics about the world production of all articles, we can determine with certainty from the available data that the world production of commodities has grown in the same scale. World production was, in thousands of tonnes:[80]

	1900	1909	Increase
Iron ore	91,888	136,500	48 per cent
Pig-iron	40,726	61,000	50 per cent
Coal	725,000	980,000	35 per cent
Copper	529	853	61 per cent
Petroleum	191,659	361,400	88 per cent
Wheat	75,710[81]	99,130	31 per cent

[79]The estimated numbers from Lexis.

[80]*Compass, Finanzielles Jahrbuch für Österreich-Ungarn*, 1911, and *Statistisches handbuch für das Deutsche Reich*, 1910.

Cotton	15,513	22,467	45 per cent

Since, therefore, the production and transport of the other commodities in recent years, as the statistics of the main types of goods shows, has at least increased to the same extent as the growth in the mass of gold employed in the settlement of exchange transactions, the high cost of living of the last years cannot be explained, even on the incorrect basis of the quantity theory, by the increase in gold production.

We go the extra mile by still adding that the increase in gold circulating medium could only bring about the rise in prices if the whole exchange of goods were mediated by actual gold. Now, it is common knowledge that most commodity exchanges are not settled through the mediation of actual gold, but with the help of gold tokens (cheques, banknotes, clearing), partly because of their easier handling, and partly – as times of crisis strikingly show – from absolute lack of actual gold, as is currently the case. The increase in world gold stocks would therefore lead, not to a rise of commodity prices, but to the displacement of an aliquot part of the gold tokens by actual gold.

* * *

We now turn to the question of *whether a cheapening in the cost of production of gold may have caused the current rise of prices*.

If the production of a kilogram of gold – by the application of new machines – becomes cheaper, if a unit of weight [of gold] contains less socially necessary labour time, the depreciation of gold must readily be transferred to the gold coins serving as measure of price, because the various central banks absorb raw gold at a fixed price, that is for a fixed number of gold coins, and moreover because the British, American and Australian mints are required to coin raw gold on demand for free or for a minimal stamping fee. 'The price of gold, measured in coin of the same metal, of equal fineness, can never vary'.[82]

If the value of raw gold decreases, this reduction in value transfers itself completely to the gold coins, and since those coins constitute the measure of value, their depreciation must announce itself through a general price rise of all commodities – not only of those goods that are exchanged against actual gold payment, but of all goods, because gold coins are used as 'ideal money of account' for any transaction.

From many reports in recent years, it is clear that new machines were really used in the production of gold and cost savings have been achieved. Inflation is thus partly due to this fact.

[81]Average of the years 1898 until 1902.
[82]Fullarton quoted in Hilferding 1981, p. 53.

That is the theory whose accuracy nobody questioned. Otto Bauer says, for example:[83]

> *The reduction in the cost of gold extraction in the South African gold mining industry is probably one of the causes of today's rise of prices.* We must now give in exchange for each commodity more money, more gold, because every piece of gold today embodies less social labour than before.

Verisimilar as this argument may sound and generally accepted as this view is, *we cannot deem it right for the following reasons*:

It is a well-known fact that the prices of commodities are only determined by the socially necessary labour time contained in them if their number can be increased in line with demand with no increase in production costs. The prices, however, of those goods that can be produced in increased quantities only with higher production costs are determined by the costs of production of that amount still required to satisfy all the demand that is produced under the worst conditions of production. This is the case with the products of agriculture. 'The production price of the worst soil that yields no rent is always the governing market price'.[84]

The introduction of a labour-saving machine, a technological innovation reduces the market price of commodities of the first class in general: the new mode of production becomes social, and therefore price-determining. In contrast, if such an innovation is introduced in a production area where the price of production of the worst, yet necessary, quantity of goods controls the market price, *the market price will only fall if, through the innovation, also the regulating price, the cost of production of the commodities manufactured under the worst conditions, falls*. If that is not the case, then the old market price will remain unaltered, and the result of the innovation will only be an increase in the surplus profit of those who produce under the more favourable conditions of production.

Those who claim that the newly-introduced machines have reduced the price of gold, make the tacit assumption that gold is a commodity whose production costs are determined by socially necessary labour time in general. However, in our opinion: 1. in gold production, just as in grain production, the amount of gold produced under the worst conditions is price-determining, and the better pits enjoy a differential rent; 2 *labour-saving innovations have not reduced the price of production of gold produced in the worst conditions, and therefore their only result has been to increase differential rent in the gold mining industry*.

[83]Bauer 1910.
[84]Marx 1981, p. 797.

The analysis of gold production proves the correctness of our assertions.

If someone wants to exploit a gold deposit, the maximum production costs are given to him in advance with absolute certainty: the production cost of one kilogram of gold cannot reach the expenditure of one kilogram of coined gold. Wherever the mining of one kilogram of raw gold costs more, the pit cannot be exploited, because the exploitation would result in a loss.[85]

But on what do the production costs of a gold mine depend? First and foremost, not on the mode of production employed, but above all on the wealth of gold content.

The production costs of gold are not calculated according to the [amount of] gold obtained, but according to the *quantity of processed ore* and the depth of the pits; with reference to gold there is absolutely no common production costs, because there are mines in which the mining and processing of the same quantity of ore yields five times more gold income than poorer mines.

If we now assume that new labour-saving methods for the mining and processing of gold ore are invented are introduced, would then the price of gold fall vis-à-vis other commodities? Absolutely not!

The only consequence of those innovations would be that now also those goldfields that had not previously been exploited can be exploited; because of the cheaper working of ores, a kilogramme of gold can now be obtained by the expenditure of a smaller quantity of minted gold. *The production cost of the price-regulating amount of gold produced under the worst conditions remains the same*; the only result would be that the previously worst gold pits yielding no differential rent now also generate one, while the rent of the pits that already yielded a differential rent would experience a corresponding increase!

A reduction in the market price would only occur if, *through the labour-saving innovations, such a large amount of newly-produced gold reached the market that part of it would become superfluous*. In that case, the price of gold would go down, and part of the mines producing under the worst conditions would stop production.

But that is not the case. The central banks of all countries eagerly absorb the amounts of raw gold offered at the previous prices; there can be absolutely no talk of a surplus, and therefore also of a price reduction. Labour-saving innovations have been introduced in the last decade, but they have only increased the mining rent without reducing the value of gold.

We could close our comments quietly with these purely theoretical considerations. But to make our views more acceptable, we want to add something more.

[85]'Gold finds its exchange value ready against the commodities, insofar as it is reflected in world commodity prices.' Lexis 1910, p. 101.

That the conditions of gold production really are as we described them is proven by the fate of the gold mining enterprises. About half of the new gold mines have to close the operation in the shortest possible time because production costs exceed the sale price;[86] while others exploiting rich ore reap exorbitant profits, which obviously come from a differential rent.

In order to illustrate how uneven the yields of gold mines are, we reproduce here the dividend statistics for some South African gold mines:[87]

	1901	1902	1903	1904	1905	1906	1907	1908	1909	1910
Anglo-French Exploration	8	27½	17½	-	20	-	-	-	10	12½
Consolidated Gold	-	25	-	12½	15	-	12½	20	35	35
East Rand	-	-	25	20	20	-	45	42½	40	40
Ferrreira	-	100	187½	250	262½	300	300	300	600	300
General Mining	-	10	10	-	20	-	-	-	5	15
Globe and Phoenix	50	35	-	-	22½	27½	15	22½	35	125
Premier Deferred	-	-	-	-	400	400	400	-	200	200
South African Gold	50	50	-	12½	15	-	-	10	25	25
Rand Mines	-	80	-	100	100	180	130	190	350	220

We see that the dividends of the gold mining enterprises vary between 0 and 600 per cent; there are mines which in ten years paid 70 per cent and those who paid 2,600 per cent in dividends. That is only possible in a branch of production in which there is a fixed sale price but very fluctuating production costs, and where the fixed sale price is determined by the amount of goods produced under the worst conditions.

Those who claim that the rise in prices of recent years is due to the cheapening of gold production have to demonstrate the economic mechanism through which the reduced production costs [of gold] could assert themselves in [commodity] prices.

In commodities which can be increased without limit, the reduction in production costs

[86]See extensively in Epstein 1909.
[87]Deutscher Börsenkalender 1911. Beilage der *Frankfurter Zeitung*.

manifests itself, through the competition between the companies that first introduced the new methods [of production], in a reduction in prices. Competition forces the other enterprises either to reduce prices or to lose their customers, since the competing enterprises can potentially provide the entire market with goods.

In the production of the commodity gold, there is no competition. The kilogram of the new, *more cheaply produced* raw gold is bought by the central banks with the same number of gold coins or the same proportionate amount of commodities as before. The price of the vast amount of gold, accumulated for centuries and having a fixed exchange rate with all commodities, is not affected by the reduction in the production cost of gold.[88] The cheaper production increases the differential mining rent; here there is no competition: the profits made through the reduction in production cost flow as surplus profit into the pockets of the mining capitalists.

Otto Bauer himself seems to have had an inkling of this state of affairs, because in addition to the above-quoted reasoning he advanced a second one to explain the rise in prices allegedly brought about by the reduction in the cost of production of gold. He says:

> The gold mines owners supply the extracted gold to the mints and banks. They receive in exchange for it coins or bills of exchange, instructions [*Anweisungen*] on gold, with which they first of all defray the costs of production of gold. The excess of the amount of gold produced over the production costs remains theirs. It is all the greater, the lower the production costs.[89]

We see here that Bauer presupposes the existence of a fixed price of gold, independent of its cost of production, in contrast to his later statements, according to which the fall in production costs automatically brings about a decline in the purchasing power of gold! He then continues as follows:

> With this surplus they then buy commodities. The gold producers do not increase the stock of commodities because they produce gold, not commodities; but they increase the demand for commodities. They increase it all the more, the greater the excess of gold production over the costs, thus the lower the costs are. The increased demand for

[88]'It is self-evident that the greater the maturity of capitalist production, the greater is the quantity of money accumulated on all sides, and the smaller therefore the proportion that the new gold production of each year adds to the quantity, even though this addition may be quite significant in absolute terms' (Marx 1978, p. 549).
[89]Bauer 1910.

> commodities with a constant supply drives up commodity prices. *In this way, commodity prices are increased by the fall in the costs of production of gold.*

We see, therefore, that not the decline in the price of the commodity gold, but the increased demand for commodities at a constant price of gold is described here as the cause of the rise of prices.

However, we believe that also this argument is not cogent.

First, the increased demand of the mine capitalists reaping higher profits would only create an additional demand for *certain* goods, mainly for luxury goods, or, if an accumulation takes place, for work equipment, but not for consumption articles, clothes, housing, and so on, whose prices have all in the last decade increased so enormously.

Secondly, however, the additional surplus profit that the mine capitalists themselves reap is, at best, *vanishingly small compared to the amount of commodities exchanged in world trade*, and therefore it cannot cause a general price increase, as the following data shows:

The total value of gold produced in 1909 amounted to 1,881 billion marks.

Let us assume an extreme case: that the profits of the mining capitalists in that year were greater by as much as 25 per cent than *the total value* [of gold] in previous years. In that case, the sum of profit by which the mining capitalists increased the demand for commodities would have amounted to *470 million marks*.

But compared to the total demand of the world market this is such a vanishing amount that it cannot possibly cause an increase in commodity prices. Thus we cannot accept Otto Bauer's explanation – the only one that would be theoretically sound – and we must stick to our argument that *changes in gold production cannot be the cause of inflation*!

If the advocates of bourgeois interests continue to insist that changes in gold production have caused the high cost of living, this makes good sense for them: they want to shift responsibility for inflation on an inaccessible, distant technical factor. But for the champions of the proletarian interests this makes no sense, if my remarks are correct.

If they are not, I would gladly like to be informed about a better argument!

Chapter Five

Gold Production and Price Movements (9 February 1912)

Jacob van Gelderen

Jacob van Gelderen (1891-1940) (pseudonym “J. Fedder”) was a Dutch economist of Jewish extraction. In his youth he was active in Poale Zion, but he later joined the left wing of the Social Democratic Workers' Party of the Netherlands (*Sociaal Democratische Arbeiders Partij*, SDAP). He is best remembered today for proposing the existence of hypothetical 50- to 60-year long economic cycles known as “Kondratiev waves” (Gelderen 1913). He worked between 1911 and 1919 in the Bureau of Statistics of the City of Amsterdam, and in 1919 he travelled to the Dutch East Indies in order to build a new Statistical Service Department for the Ministry of Agriculture, Industry and Commerce. In 1925 he became the first director, until 1932, of the Central Bureau of Statistics in Batavia, the capital city of the Dutch East Indies. In 1928 van Gelderen was appointed extraordinary professor of political economy at the Law School in Batavia. By then the former Marxist had become an outspoken critic of Karl Marx and the labour theory of value. In 1933 he returned to the Netherlands and was the Colonial Head of the “Crisis Affairs Department” (*Crisiszaken*), which also covered economic relations with the Dutch East Indies. To combat the Great Depression, van Gelderen supported the Plan for Work commonly known as the Plan de Man after its creator, the Belgian politician Henri de Man. Van Gelderen joined the Board of Trustees of the Scientific Office of the SDAP, and helped draft the so-called Labour Plan of 1935, of which he wrote the chapter on Indonesia. In 1937, van Gelderen was appointed professor of sociology at the Faculty of Law of the University of Utrecht. In May 1940, during the Nazi invasion of the Netherlands, he committed suicide together with his wife and their two youngest children. This article is a refutation of Varga’s claim, made in the previous item of this collection, that gold production cannot affect the general price movement and therefore could not be one of the causes of pre-WWI inflation.

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In No. 7 of the current volume of this journal, comrade Eugen Varga has undertaken to prove

theoretically that today's rise in prices, which has taken hold of almost the whole world, cannot be attributed to changes in gold production. If he had only said that, I would have made no attempt to dispute his conclusions, because I think that nothing certain can be said today about this particular issue. He believes, however, that he has also furnished the proof that the often mentioned link between gold production and the general price movement does not exist.

In my opinion, if he were right in his allegations, the foundations of the contemporary monetary system and one of the main principles of Marxism would become invalid, and it therefore seems not without benefit to emphasise the logical error he is guilty of in his article.

According to Varga, cost reductions, that is labour savings, do not depress the value of gold. That is because gold is not one of the commodities for which the minimum cost law applies; gold is one of those goods whose number can be increased only at an increased cost expenditure, like the agricultural products.

From this follows, according to Varga,

> that '*labour-saving innovations have not reduced the price of production of gold produced in the worst conditions, and therefore their only result has been to increase differential rent in the gold mining industry*'.

I cannot agree with this argument. It totally fails to recognise the price laws of the commodities that cannot be replicated *ad libitum* [at (one's) pleasure]. It has never been argued that an increased productivity of agricultural labour, assuming the existence of competition, does not cause a fall in prices. Each producer continuously strives here, just as in industry, to lower his price of production below the social one, and if he succeeds, he will be able to supply the market with a larger quantity of his product than before. *Ceteris paribus*[90] the price must consequently decrease, and the producers working under the as yet most adverse circumstances will, if they do not want to make a below-average profit, have to stop their production.

Incidentally, Varga also remarks that, as a result of rising demand, and therefore of rising prices, differential rent for the most favourably situated producers must increase (or come into being), whenever the expansion of production can take place, only with higher costs. Not rising, but falling productivity increases the rent [according to Varga]!

Varga thinks he must emphasise that the production costs of a gold mine depend 'first and

[90]In a deduction it is entirely justified, indeed necessary, to presuppose as constant all other factors that influence the process discussed.

foremost, not on the mode of production employed, but above all on the wealth of gold content'.

Does he not see that, for the question under consideration, the effect must be the same in both cases? In the theory of value, the wealth in gold content appears precisely as the amount of gold to be produced with a determined quantity of social labour. This subject is discussed by Marx in *Capital*,[91] where he discusses the value formation of agricultural products.[92]

In this context, continues Varga:

> The production cost of one kilogram of gold cannot reach the expenditure of one kilogram of coined gold. Wherever the mining of one kilogram of raw gold costs more, the pit cannot be exploited, because the exploitation would result in a loss.

I don't think we have here a special case for gold producers. The only circumstance that could be confusing here is this: in the process M – C . . . P. . . C' – M' in the production of gold, C' is at the same time M' (as Marx already indicated). The gold producers are not forced to make their goods go through an economic formal transfiguration again in order to get back their capital in the form it had at the beginning of the stage of the reproductive process considered in isolation. But this formal peculiarity exerts no effect on value formation.

Varga cited Wilhelm Lexis, the monetary theorist: 'Gold finds its exchange value vis-à-vis the commodities ready-made, insofar as it is mirrored in world trade prices'.

But this sentence says something quite different from what Varga wants to see in it. It refers precisely to the above-mentioned fact that the gold producer cannot learn the exchange value that his product will realise immediately, from the market quotations (as is the case with producers of other goods), but only indirectly, from the general price level. For better illumination of this point I would like to add here what Eugen von Philippovich [1858–1917] says in his famous *Grundriß der politischen Ökonomie*, page 246, because is clearly shows Varga's error. He says:

> For example, if the production and procuring a pound of gold costs more than 1,395 marks, it is no longer worthwhile, because at any time, from the circulation of gold of all states, this quantity of gold can be obtained from the given number of gold units. In the last analysis, the monetary standard ratio is therefore the maximum limit for the

[91]Marx 1976, p. 130.

[92]See also Marx 1981, p. 213: 'It is particularly agricultural products, whose raw materials derive from organic nature, that are most subject to these fluctuations in value, as a result of variations in the harvests and so on'.

> price of precious metals.

We see, however, how ill-conceived the last sentence is. The monetary standard ratio, that is the legally established number of gold coins to be minted from a given weight of gold, would affect the value of gold! In round, gold-stamped discs, gold is therefore something else (maybe finer, more valuable?) than in crude bullion. With just as much right you might say, 10 decilitres of water determine the maximum weight of a litre! Even Varga – who however quotes Marx's sentence: 'The price of gold, measured in the coins of the same metal, cannot vary' – falls back into this error when he writes:

> In the production of the commodity gold, there is no competition. The kilogram of the new, more cheaply produced raw gold is bought by the central banks *with the same number of gold coins or the same proportionate amount of commodities* as before. (Emphasis mine.)

In the same breath Varga mentions two entirely different events as evidence in favour of the same claim. For one kilogram of gold the same number of coins will always be given, whatever the value of gold. This parity (abstracting from the minting cost) is precisely the term that binds together the prices of commodities expressed in a particular currency with the commodity gold (their measure of value).[93] '*Or the same proportionate amount of commodities*' is something completely different. Only according to this standard we can recognise the value movement of gold.

I also have reservations about another aspect of Varga's statements, namely: does gold belong entirely to the type of goods which, like agricultural products, can be produced in larger quantities only at disproportionately higher costs? Yes and no.

Yes, insofar as with the usual mining methods, one has to penetrate further and further into the soil when the already broken in veins are exhausted. No, to the extent that one has the degree of mining under control, because here the production technology and the capital employed are the only determining factors.

Varga himself mentioned the case in which increased production reduces the value of gold. He says:

> A reduction in the market price would only occur if, *through the labour-saving*

[93]We may abstract entirely from the tiny 'exchange rate' [*kurs*: course]-fluctuations of gold, which manifest themselves in oscillating gold quotations of various currencies [*Münzsysteme*: coin systems].

> *innovations, such a large amount of newly-produced gold reached the market that part of it would become superfluous* . . . . But that is not the case. The central banks of all countries eagerly absorb the amounts of raw gold offered at the previous prices; there can be absolutely no talk of a surplus, and therefore also of a price reduction.

Here, gold as a measure of value (that is, as a commodity with a value of its own) is confused with gold as a general form of commodity wealth and as material for coins.

Precisely because gold, in addition to its use for industrial purposes, always functions as the foundation of the monetary commodity exchange, the big central banks always accept it. They, as 'delegated public enterprises', must always strive to keep the national monetary and credit system undisturbed. Through their metal treasure they make possible: 1. the convertibility of their notes, 2. the potential export of gold to foreign countries if the exchange rates reached or exceeded the upper gold point.

Whatever the value of gold, in other words, whatever the height of the general price level, so long as gold is the money metal, it has for the central banks this eminent significance.

Even more unfortunate is Varga, in my opinion, in his quotation of the mine dividends table on page 218. If what he argues, that the least productive gold mines have to close down operations in the shortest time, were true, from this would merely follow the conclusion that, when faced with inflation, the value of the gold producers' product falls more and more. The weaker brothers fall in battle.

For the rest, the table coveys very little, since one would have to know a number of factors exactly in order to assess the meaning of these figures. For example: to what extent is the dividend policy a kind of stock-exchange speculation; are the mines paying low dividends perhaps repaying large loans; do they use their profits to increase the scale of their operations, and finally, do the very profitable companies have some kind of legal or other type of monopoly?

One more point I want to touch briefly, namely Varga's claim that the conceding of a relationship between gold production and the rise of prices relieves the theoretical representatives of bourgeois interests of a heavy load. No way! Except that the Social Democrat, in that case, does not to turn against this or that particularly usurious capitalists group, but against the current economic system in general. The rise of prices surely illuminates most clearly how much the workers are afflicted by the uncontrollable vagaries of production!

Whether the *current* rise of prices is caused by changes in gold production, I leave

undecided; that such an effect is possible is – in my view – indisputable.

Chapter Six

Money and Commodities[94]

(1 March 1912)

Rudolf Hilferding

Rudolf Hilferding (1877–1941), like Otto Bauer a prominent Austro-Marxist, was, like Bauer, born in Vienna into a prosperous middle-class Jewish family. He joined the Austrian Social-Democratic Workers' Party (*Sozialdemokratische Arbeiterpartei Österreichs* or SDAP) in his student days. Whereas Bauer earned a Ph.D. in Law, Hilferding studied medicine at the University of Vienna. By 1902, however, his brilliance in economics was such that Karl Kautsky invited him to become a contributor to the SPD's theoretical journal *Die neue Zeit*. In 1904, together with socialist friends from university days—Max-Adler, Otto Bauer and Karl Renner—Hilferding founded a socialist publishing enterprise called the *Marx-Studien* series. The first published volume of *Marx-Studien* was Hilferding's reply to Eugen von Böhm-Bawerk's *Karl Marx and the Close of his System* (Hilferding 1904). Unlike Bauer, who stayed in Vienna, Hilferding moved in 1906, at Kautsky's initiative, to Berlin, where the taught political economy at the SPD's party school. He was forced to give up this job because of a law forbidding the employment of teachers without German citizenship, but he remained in Berlin as editor of the SPD central daily paper *Vorwärts* and a regular contributor to both *Die neue Zeit* and the theoretical organ of the SDAP, *Der Kampf*. There he completed his major work, *Finance Capital*, which was published in 1910 as the fifth volume in the series of *Marx-Studien* (Hilferding 1981). In this article, Hilferding agrees with Varga's argument that 'changes in gold production cannot be the cause of the rise in prices', but from a different theoretical perspective, already developed in *Finance Capital*: the idea that, under inconvertible paper money, the "exchange rate" between money and commodities is determined by the "social necessary circulation value"—i.e. by the total value of the commodities in circulation. This theory was premised on the idea that there could exist a "social regulation of commodity circulation" under capitalism —that is to say, that the bourgeois state could somehow tame, by means of the central banks, the anarchy of capitalist production. In that sense, it was a forerunner of Hilferding's theory of "organised capitalism," which he however fully laid out only when he had already

[94]Hilferding 1912a.

broken with revolutionary Marxism (see particularly Hilferding 1915 and Hilferding 1924).

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In his interesting article 'Gold Production and the Rise in Prices', comrade Eugen Varga defends the thesis that 'changes in gold production cannot be the cause of the rise in prices'. We are of the same opinion, but we believe that Varga's argumentation, to be conclusive, still requires a substantial addition.

Varga begins by disposing of the quantity theory, whose profound content has recently been reproduced by *Simplicissismus* [a satirical German weekly magazine] just as correctly as comically as follows: 'The colossal production of gold has thrown so much money into circulation that prices have increased so much that not enough money is available to pay for the commodities.'

The quantity theory is as primitive, simplistic and wrong as the population theory of Malthus, and therefore just as long-lasting. Except that the quantity theory has received, through the experiences with restricted currency, some semblance of justification, which the Malthusian theory lacks at all – at least in the eyes of superficial observers, who fail to see precisely the essential. Because precisely the phenomena of the restricted or of a pure paper currency can only be understood if the *value* of the mass of commodities in circulation is determined objectively, that is, it can only be understood with the help of the labour theory of value. Because the worth [*Geltung*], the exchange rate [*Kurs*] of inconvertible paper money is determined by the value of the circulating mass of commodities, it is a reflex of the total value of the commodities in circulation. This must be objectively given so that a standard of comparison can be found at all between the mass of commodities in circulation – and one can add up the commodities only as values – and the monetary units. The quantity theory becomes, however, completely absurd in a free[95] gold currency.

> The illusion that it is ... prices which are determined by the quantity of the circulating medium, and that the latter for its part depends on the amount of monetary material which happens to be present in a country, had its roots in the absurd hypothesis adopted by the original representatives of this view that commodities enter into the process of circulation without a price, and money enters without a value, and that,

[95][That is, with unrestricted coinage.]

> once they have entered circulation, an aliquot part of the medley of commodities is exchanged for an aliquot part of the heap of precious metals.[96]

But since a theoretical argumentation is not everyone's cup of tea, Varga has earned credit for having once again demonstrated statistically the nonsense of the quantity theory of money. The real world-economic causes that have led to the rise in prices and that must be looked for on the *commodities'* side, not on the side of the production of gold, have been systematically presented by Otto Bauer in his brochure on the rise in prices. There is no doubt that the reasons adduced there are entirely sufficient to explain the rise in prices.
Varga then goes on to investigate the question of whether a fall in the cost of production of gold manifests itself in the price of gold. The question under consideration is of course not its nominal price. Since a pound of pure gold must always, under the provisions of the law, be stamped 1,395 marks, the 'price of gold' is nothing but the expression of a certain quantity of gold, and a mark is just another expression for 1/1,395 pounds of gold, that is, first of all, a weight designation, not a price expression. This price expression is first given to us when we read a catalogue of prices backwards and infer from it, that 10 marks gold are equal to *a* meter fabric, *b* kilograms of salt, *c* pair of gloves, and so on.
Now Varga's statement means that, whatever the production costs of 10 marks of gold, they will *always* be exchanged for *a* meter fabric, *b* kilograms of salt, etc., assuming that the conditions of production of salt, fabric, etc. remain the same. This thesis thus seems at first sight to contradict any theory of value, and Jacob van Gelderen gives in his article a clear expression to this concern. Now certainly, says Varga, the changes in the cost of production of gold exert no influence on [its] exchange value because gold is one of the commodities for whose price formation the laws of ground rent are decisive. For such goods, the price of production of that amount of commodities is determining, which has been produced under the most unfavourable circumstances, assuming that demand still requires that amount of goods. A cheapening of production would lead at most to a rise in ground rent, but not to a fall in the price [of gold]. Now the question is precisely whether such a cheapening [that is such a reduction in the cost of production] has occurred, so that the amount required by demand can be produced under better conditions of production, that is whether, for example, as a result of the improvements in technology and the discovery of the South African mines the same thing has happened for gold as occurred to wheat as a result of the improvement in the means of transportation and the resulting American competition, or to

[96]Marx 1976, p. 220.

silver at the time of the discovery of the American mines. For in the latter case, as can hardly be doubted, actually the rise in prices did develop as a consequence of a depreciation of the currency.

Now, Varga himself has hinted at the crucial point, but refrained from elaborating it, which is the reason why also Jacob van Gelderen completely overlooked it. It is the 'unlimited demand' for gold and the peculiar regulation of the monetary system by the central banks. In *Finance Capital* I pointed out, that with restricted or paper currency, the value of money is determined by the 'social circulation value'. That is, the value equation in this case is as follows:

> The value of the money sum = (total value of commodities)/(velocity of money circulation) plus the sum of payments falling due minus the payments which cancel each other out, minus finally the number of turnovers in which the same piece of money functions alternately as a means of circulation and as a means of payment.[97]

What happens now with today's free gold currency? Gold has a determined intrinsic value. But the previously postulated equation must also hold for the amount of money actually used for circulation purposes. With restricted or paper currency, the whole mass of money tokens [*Geldzeichen*] goes into circulation; because under-valued metal money or paper money is not suitable for other purposes, at least under the given historical conditions. Such money first receives its exchange rate [*Kurs*] through the social circulation value.

The situation is different with free gold currency. Assuming that society disposes of a gold stock of 2,000; if the circulation value equals 1,000, then gold pieces worth 1,000 will be in circulation, while 1,000 will be kept as hoard.[98] Here, because the amounts of gold have their own value, the circulation value determines the *amount* of gold pieces in circulation. With restricted or paper currency, the amount [of paper money in circulation] is given, and its value is determined by the total value of the commodities in circulation, while with a gold currency the intrinsic value of gold is given, and the *amount* [of gold pieces in circulation] is determined by the circulation value.

But now a specific mechanism has been created by the major *central banks* for the entrance or exit of the gold respectively necessary or unnecessary for circulation. Central banks accept all the gold offered to them. The demand is therefore *unlimited*. But a price change takes

[97]Hilferding 1981, pp. 47–8.

[98]Gold can only function as hoard, as general incarnation and means of storage of social wealth, because it has an *instrinsic value* as opposed to paper money.

place only as a result of a shift in the ratio between supply and demand. The demand is now in fact unlimited. At first this only means that for 1 kilogram of gold always 1 kilogram in gold coins will be given. This new kilogram initially disappears in the vaults of the central bank and is stored there as treasure (reserve). Let us suppose that the circulation value grows from 1,000 to 1,500. If there were no gold reserve, the exchange rate of the gold coins would have to change; 1 mark would be now worth 1½ mark, and vice versa. But the central bank also accepts every redundant gold piece in circulation and adds it to its reserve; a change in the value ratio [between money and commodities] cannot therefore develop at all.

For changes in the value of gold to manifest themselves, gold must remain in circulation. Only when commodities and means of circulation face each other *directly* can they mutually determine their values. Money outside circulation – as reserve in the central bank's vaults – stands in no ratio to the sum of commodities in circulation.

The actual sequence of events is therefore this. The producer of gold receives 1 kilogram of gold coins for 1 kilogram of gold. The new gold lies in the central bank's vaults. If circulation needs increase, gold flows from the bank's vaults into circulation. *Thus the rate of exchange between gold coins and commodities always remains as it was at the beginning of the process*. Changes in gold production have no effect on this ratio, as long as this mechanism remains intact. It would change immediately as soon as the mechanism was abolished. Let us assume that gold production grows so quickly, that the central banks find the accumulated gold reserve sufficient for all their purposes. In that case, they would refuse to accept gold from a certain date on. Since they would continue to regulate circulation in the same way as before, accepting all the minted (coined) gold in circulation and making available out of their reserve the coins becoming necessary, the exchange ratio [*Tauschverhältnis*] of minted gold [with the commodities] would not change. It would be otherwise with gold as a commodity. The unlimited demand would cease. Gold would now be primarily demanded for luxury and industrial purposes. The previous supply would become too large for the reduced demand. Competition would ensue among gold producers, the price of gold would fall, gold mines producing in the most unfavourable conditions would have to stop production, and total gold mining rent would fall sharply. These are processes that have actually taken place in a similar manner with the demonetisation of silver.

The gold currency would become, in fact, a restricted currency; the exchange rate [*Austauschverhältnis*] of the gold coins [with the commodities] would be different from that of unminted gold (bullion); the former would remain the same despite the fall in gold prices – again, all events that have occurred with restricted silver currencies.

But even if the exchange rate of the gold coins [with commodities] remains the same, yet another function of the gold reserve of the central banks would be disturbed. Marx has already pointed out that this gold reserve has several different functions subject to completely different laws. The gold hoard [of the central banks] is not only a reserve for circulation; a guarantee, even if only virtual, for the convertibility of the money claims [*Geldforderungen*] into gold; it is also a fund for the settling of international balances and a means of storage of wealth in its ever-exchangeable form. Now, the state stamp that turns gold into coins holds only within the state borders; in order to settle the international balances, gold is only worth according to its metal value; if that value is detached from its value as coin – which would happen with the restriction of currency – the reserve of the central bank could be also reduced in value, insofar as it serves to balance international payment differences. Only an international regulation of currency, which would thus provide a single uniform economic territory for monetary circulation, would prevent this consequence. But the nation-state antagonisms disrupt international regulation; if not earlier, a state of war would throw such an international agreement into disarray. That is the reason why a change in the unlimited demand for gold must be ruled out. By contrast, the two other functions of the gold reserve [of the central bank], if it is large enough – that is: reserve for circulation and guarantee fund for the convertibility of the outstanding debts into gold, and moreover into gold *coins* – could be fully met even with such a restricted gold currency.

That the direct application of the law of value for gold as money is abolished, and that this law determines the exchange rate [*Kurs*] of money (as we prefer to say here rather than value or price of money) only indirectly, through the mediation of the social circulation value, is at bottom, striking as this phenomenon may seem at first glance, nothing wonderful. The law of value requires total economic freedom for its operation, but this freedom is modified for the exchange rate between money and commodities by the operation of the central banks. The specific nature of money makes it difficult to offer an illustrative example, but let us imagine the following situation: in a completely closed, autarchic economy the state introduces a monopoly of oil trade. Let us say that it constantly keeps a reserve of 100 million litres. The state sells 100 litres of oil at a price of 30 marks to everyone, and it is always ready to buy the oil offered to it at a price of 29½ marks. The consequence would naturally be a constant oil price of 30 marks. This price would decide what oil fields could be exploited, which oil fields would yield a rent and how high those rents would be. A growing demand for oil would be met from the reserves, and the 'policy of the oil bank' would take care of securing this always

sufficient magnitude. If the demand decreases or production is especially abundant, the reserve also increases, which would be considered an especially favourable circumstance by the bank managers. The sequence of events with gold is entirely analogous, only that in this case the invariable exchange relation [between money and commodities] can with compelling certainty be proved only theoretically.

But if these theoretical conclusions are correct, a further conclusion follows. If the exchange rate between gold and commodities is stable, the same regulation must obviously have the same effect with silver. In that case, however, since it is a question of two constant magnitudes, also the ratio between gold and silver would remain constant, and the possibility of bimetallism would be theoretically proved. I hasten to add that I never linger on practical consequences; even less would it be possible, as can be seen from what follows, to arbitrarily change this ratio in favour of silver. But from a purely theoretical point of view a dual currency would be conceivable, provided that the central banks internationally accept silver just as unlimitedly [as gold] and hoard it in case of need just as they do with gold.[99]

To raise yet another 'academic question': what effect would now a trust have on gold production? It would generally first become effective, when the central banks have reason to fear that their accumulated gold holdings are no longer sufficient to make up for their international obligations; in that case they would be forced to pay for 1 pound of gold more than 1 pound in coins, that is for example, more than 1,395 marks. If they do not change their mechanism for satisfying the circulation needs, they would suffer losses to the extent of their gold purchases, and this could be the only effect. Probably the central banks, in order to protect themselves from a drain of gold, would raise the interest rate. But the increase in interest rates as such has no effect, at least not directly, on the level of commodity prices, even if vulgar economics considers this self-evident, because it rates the interest rate among the 'production costs'. The only means that the central banks would have to adjust the exchange rate of gold [*Goldkurs*] to the monopoly price would be their refusal to satisfy the circulation needs to the same extent as previously – by restricting the currency, that is by changing the whole mechanism. In reality, however, the gold trust would long have foundered on the power of the central banks, behind which indeed stand the states themselves.

If, given a free gold currency, that is an unlimited acceptance of the gold production by the central banks, the exchange rate between the gold coins and the commodities is certain and unchanging, how did that exchange rate come into being? The answer can only be that it has

[99][Hilferding is contradicting here well-known statements of Marx and Engels against bimetallism, which Engels called 'the double standard swindle' in his letter to Eduard Bernstein of 10 May 1882.]

formed *historically*, at times when gold still entered directly into circulation, when there was no social regulation of circulation of any kind, taking into consideration that the decisive thing for our problem is not the coinage (minting) by the *state*, but the fixing of the coin as a certain weight of gold, and the *acceptance of all the gold by the central bank* at that fixed 'gold price'.

Here an objection could still be raised, which at first sight seems to carry great weight. Even before the establishment of central banks or, more generally, of the state regulation of the unlimited acceptance of all the gold offered at the market, gold flew into circulation and out of it again through the transformation of hoards into means of circulation or payment, and vice versa. Was this hoarding not of the same significance for fixing the exchange rate between gold and commodities as the state regulation of circulation? However, this argument overlooks a very significant difference. Hoarding by private individuals is ruled by completely different laws than hoarding by the central banks. The central bank hoard[100] directly serves as a reserve of circulation; the central bank is committed, and it could not be otherwise, to satisfy immediately the needs of circulation as soon as they arise. The situation was completely different when that regulation did not exist. If from the circulation needs resulted that the gold exchanged for commodities grew in value, there was no reason for private persons to throw money into circulation. The treasures of the monasteries, the hoards of the rich merchants, the war treasures of the state, and so on, were not reduced in the fifteenth, sixteenth or seventeenth centuries because gold was lacking in circulation. And even today the hoards of private individuals, where they still exist, are not a reserve for circulation, but a reserve for their own solvency. In the modern economy, such private hoarding in the form of money indeed does not take place in any significant degree; hoarding, accumulation of wealth takes place here in the form of possessory titles on future production. But even if this private hoarding in money form takes place, it remains the exception, in particular a result of a critical stoppage in circulation. At a monetary crisis, which can be associated with a sudden increase and over-valuation of money, we also have accumulation of cash (gold) in private hands, and precisely this accumulation sharpens the scarcity of money; conversely, the central bank's reserves are used to make available the gold necessary for circulation.

Formerly, the entering [of gold] into circulation was not as mechanical a process as it is today. Gold back then had *no unlimited demand*. It had to be exchanged for commodities, and therefore entered immediately into circulation and remained in it, unless private

[100][*Bankschatz*: central bank reserves, rendered as 'coffers of the Bank' in Marx 1981, p. 561.]

hoarding set in. This hoarding, however, again did not depend on the circulation needs, but on the private capacity of individuals to carry out such hoarding. Historically regarded, the hoarding of states for war purposes played the most important role. But this also meant that those accumulated treasures were periodically emptied again into circulation to pay for war expenses of all kinds, and after that remained in circulation to a large extent. This, in turn, means that the exchange rate of gold formed over and over again through the real confrontation of gold and commodities in circulation, and furthermore that at that time the value of gold actually underwent fluctuations, which sprang, on the one hand, from continual disturbances of circulation, and, on the other hand, from changes in the cost of production of gold.

In the very rich economic literature on the relationship between gold and commodities, the influence of the revolution in production conditions of the money metal on the increase of prices in the sixteenth century is beyond dispute. But the verdict is completely different for the later period.

Despite all the changes in the conditions of production of precious metals, despite the fact that often, in recent periods, countries very rich in gold have replaced their metallic money by paper currency and have thrown many hundreds of millions of marks [of gold] on the world market in the course of a few years, despite all the fluctuations in the demand for gold for the needs of exchange, it is still disputed among scholars whether at the centres of international commerce, from the middle of the seventeenth to the mid-nineteenth century, the value of money changed at all.[101]

Among the supporters of the quantity theory of money, but also by other economists, attempts are always being made to trace price changes back to changes in the amount of gold produced or its production costs. The proof has always been completely unsuccessful. Tooke has provided evidence to the contrary for the earlier period. The fall of prices after the crisis of 1873 until the end of the 1880s, which coincided with a reduction in gold production on the one hand, and with an increased demand for gold for monetary purposes on the other hand, as a result of the transition of Germany to a gold currency and the suspension of free silver coinage in other states, encouraged new investigations. In Great Britain, a great deal of material was brought up before a Commission on Gold and Silver in 1886 for the determination of that issue. In the essay just quoted, Nasse provides convincing evidence that price changes are to be sought for on the side of the commodities, not on the side of money. And Lexis is also essentially of the same view.[102] On the other hand, material is to be

[101]Nasse 1888, p. 156.
[102]Lexis 1888.

found in these studies showing how stable the exchange rate between gold and commodities has been, and that such changes could not have taken place before the metal as coins really confronted the commodities in circulation. On the European markets, silver had already fallen sharply in price vis-à-vis gold; but in India it still retained its old exchange relation against commodities for a long time. Lexis says in the article cited above:

> Of particular interest were the reports that the Commission received on the influence of the fall in value of silver on the exchange of goods between England and East Asia. To begin with, the fact (which I long doubted) can no longer be denied that in India the purchasing power of silver against agricultural produce and customary labour has not significantly diminished, despite the fall in the gold price of silver that has been taking place for many years already, and that it is expected to hold its own in the near future.

Lexis then offers the following excellent explanation:

> Upon closer examination, this value continuity of silver appears, however, less surprising than it seems at first sight. A depression of the value of silver against the Indian commodities would be expected only in the wake of a significant increase in the mass of silver coins in circulation. But such an increase is very strongly counteracted in India by the custom of hoarding.

The hoards of private individuals act in this particular case, and under the specific circumstances of India, as the reserves of the central bank, preventing the entrance of silver into circulation; since the circulation needs remained the same, so does the value of the silver coins as opposed to silver in bars (bullion), which is now determined by the social circulation value. As the price of silver continued to fall, it became irrational to hoard it; its place as treasure was increasingly taken in India by gold; silver was now to be used exclusively as means of circulation; it was pushed into circulation and gradually the prices of commodities rose also in India. The discontinuation of the free coinage of silver then put an end to the devaluation of the silver *coins*.

We come to the conclusion. The state regulation of the monetary system meant a *fundamental* change in the ratio between gold and commodities. The exchange rate between gold coins and commodities was now fixed by state intervention, but *not* arbitrarily; the state

only took over a *historically and spontaneously developed exchange ratio*; it can therefore, as long as the mechanism remains the same, *not change* it. Changes in the cost of production of gold do not affect the exchange rate between gold coins and commodities; they only decide the question of what gold deposits can still be taken with a view to profit.

Gold gets, through its use as a money metal, not only a higher price than those metals without such use; that would be nothing remarkable, because its use as money means an increase in demand. It receives a *fixed price*, and this can theoretically go beyond the price of production of the gold produced under the most unfavourable conditions. Here, then, would develop a special form of *absolute rent*, probably the only form of absolute rent that really exists.

There is, however, a misunderstanding about which we must be on guard. The fixing of the price [of gold] does not consist in the fact that a pound of gold equals 1,395 marks. That is, as I said, not a price ratio, but a weight ratio. The price [of gold] is fixed only by the fact that, given an adequate reserve of gold [in the central bank's vaults], always as many gold coins enter into circulation as required by the social circulation value.

The essence of the contemporary gold currency is perhaps most clear when compared to a pure paper currency.

> A system of pure paper currency might be envisaged in the abstract along the following lines. Imagine a closed trading nation which issues legal tender [*Zwangskurs*] state paper money in a quantity sufficient for the average requirements of circulation, and further, that this quantity cannot be increased. The needs of circulation would be met, aside from this paper money, by bank notes etc., exactly as in the case of a metallic currency. By analogy with most modern central bank legislations, the paper money would serve as cover for these bank notes, which would also be covered by resources of the banks.[103] The impossibility of increasing the supply of paper money would protect it against depreciation. Under such circumstances, paper money would behave as gold does today; it would flow into the banks or be hoarded by individuals when circulation contracts, and would return to circulation when that expands. The minimum of circulating media required at any time would remain in circulation, while the fluctuations in circulation would be covered by an expansion or contraction of bank notes. The value of the state paper money would therefore remain stable.[104]

[103][*die im übrigen bankmäßig gedeckt seien*.]

[104]Hilferding 1981, p. 57. The remarks of this essay are only inferences from the laws developed in my book.

In exactly the same way does the value of the gold coins remain stable today, except that gold, in contrast to paper money, has its own value. This intrinsic value, however, would be different without the use [of gold] as money; it would be lower and always fluctuating with the cost of production. The value of gold [coins] remains stable through a mechanism introduced by the state, the same as in the case of a pure paper currency. Only that, with the introduction of a pure paper currency, the social circulation value could directly determine the exchange relation of the paper money. With the gold currency, that exchange relation was already historically given, and the social circulation value determined, at that given stable and permanent ratio, the amount of real gold always circulating, assuming an unchanging degree of use of credit money, and so on.

This is then the effect of the 'unlimited demand' for gold [in countries with a gold currency]. It brings about the *stabilisation of the exchange relation of gold coin* and *therewith* of gold bullion, as long as the continuous conversion of gold into coins is guaranteed by law. But with this we also have actually had, ever since the general introduction of the modern gold

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Reading *Allgemeinen Volkswirtschaftslehre* of Lexis (1910) I can, incidentally, notice with satisfaction that even this important representative of a 'metallist', as Knapp would say, or a gold-fetishist monetary theory, as I would prefer to say, under the impression of the new experiences appears to be quite shaken in his previous views. On page 113 Lexis admits the theoretical possibility of a pure paper currency, which he constructs in quite the same way as I did in *Finance capital*. And this is done by the same Lexis, who only a few years ago had almost seen the start of a deterioration of the currency [*Geldverschlechterung*] in the introduction of small denominations. And shortly before that Lexis declared:

'The previously prevailing opinion that inconvertible paper money [*Zwangspapiergeld*] always remains dependent on the metal value which it originally represented has been refuted by experience. This paper money completely detaches itself from its original metal base; it not only can sink under it, but also *rise above* it. In Austria, in 1892, the exchange rate of the paper guilder against the mark was 168 to 170 pfennigs, while the value of the silver contained in a silver guilder was 130 to 140 pfennigs. But as a coin the silver guilder was equivalent in domestic trade to the paper guilders, because it could replace them in all payments. It therefore leaned towards the money paper guilders, which had become the main currency [*Hauptgeld*], while according to the older view, the opposite should have occurred. Likewise in Russia, at the time of the transition to the gold currency, the exchange rate of the paper rouble was considerably higher than it would have corresponded to the value of the silver contained in a silver rouble.'

But when Lexis as a result wants to give paper money the character of an independent measure of value, he leaves completely unexplained the main question, namely how does a worthless thing obtain value. Because the state decree, that debts must be paid in paper, could at most make plausible, that paper money will be transacted at some exchange rate [*Kurs*], until the assumed obligations are met; but it can never explain why paper money at any time has a specific and often long constant exchange relation [*Austauschverhältnis*] with commodities. In reality, paper money or metal money with restricted currency is never an independent measure of value, but its exchange rate is determined by the social circulation value. For this conceptual recognition, however, the objective, Marxist value theory is indispensable.

To avoid misunderstandings, it should be emphasised that *historically* the metallic currency must lead the way before paper currency is possible. First a commodity must have become money in the process of direct commodity exchange, in order that coin, by social convention or state law, may develop from the money commodity. And in addition to the metallic money, the circulation of (private) money tokens must have already emerged from the needs of circulation, so that the state has the possibility of replacing metallic money by its money tokens and give them under circumstances forced currency [*Zwangskurs*]. But once this happened, the measure of value changes as a result. Similarly, the state regulation of metallic money circulation requires a special modification in the application of the law of value, which leads to a special law for the price of gold as a monetary metal. Just as little as, for example, the price of production, does this special law of prices mean the abolition of the law of value. Rather, it can only be understood on its foundation and derived from it.

currency systems, a *fixed measure of value*, which the economists looked for so long but which they still did not recognise, when they already had it for a long time.

Chapter Seven

Gold, Paper Currency and Commodities[105]

(15 March 1912)

Karl Kautsky

Kautsky first stated his misgivings about Hilferding's theory of money in his laudatory review of *Finance Capital*, which he praised as "a continuation of Marx's *Capital*" (Kautsky 1911, Vol. 29 No. 1, p. 771). He highlighted Hilferding's introduction into Marxist economic literature of new theoretical concepts, such as the *founders' profit* accruing to individual capitalists turning their enterprises into joint-stock companies (which explains their eagerness to turn to the stock exchange) and *finance capital* (capital in money form at the disposal of the banks, which is made use of by the industrialists and thus actually converted into industrial capital). However, Kautsky added, "now and then Hilferding not only goes ahead of Marx, but deviates from him." He remarked that this only happened on special questions, on which Hilferding also said mostly "remarkable and true things," with one notable exception: Hilferding's theory that the "exchange rate" between inconvertible paper money and commodities is determined by what he called the "socially necessary circulation value." Kautsky called Hilferding's attempt to detach paper currency from its connection with gold a "Marxist suicide," because it "would mean the negation of the law of value for the money commodity; it would be saying that the value of the latter is not determined by the socially necessary labour time needed for its own production." Thus was the question laid to rest by Kautsky. Shortly thereafter, the debate on the Marxist theory of money broke out in the pages of *Die neue Zeit*. The exchange opened with the two previous items by Eugen Varga and Jacob van Gelderen, and was continued by the previous article by Hilferding, which forced Kautsky to state in a more detailed way the grounds for his theoretical divergences with him. According to Kautsky, Hilferding's whole theory, which regarded gold as a 'detour' in the determination of prices under an inconvertible paper currency, was built on a confusion of value (the amount of socially necessary labour contained in a commodity) and price (a determined magnitude of value expressed in a certain quantity of gold, against which it is exchanged). Actually, Kautsky argued, commodities *cannot* get a price before determining the value of money. Price is the

[105]Kautsky 1912.

> expression of the value of a commodity in money, and therefore presupposes that money itself has a value, i.e. a metallic basis in gold. The sum of prices presupposes not only a certain value of commodities, but also a certain value of gold. Gold always remains the basis of value measurement; it cannot be eliminated as a measure of value. According to Kautsky, token coins function merely as means of circulation, not as measure of value. Money has to have an intrinsic value, and this intrinsic value determines commodity prices (the monetary expression of their values) and with them the amount of money required commodity the circulation. Hilferding's theory of circulation value was just an unconscious variation of the vulgar quantity theory of money. And the "social regulation of circulation" which the central banks supposedly introduce instead of the former anarchy of circulation was, in Kautsky's opinion, just an illusion of Hilferding, just like the "unlimited demand for gold" that they supposedly generate. Actually, central banks merely centralise the function of hoarding. Kautsky concluded that commodity circulation was "determined by the needs and results of the production process, and as long as private property in the means of production holds good for the process as a whole, a social regulation of part of it is out of the question."

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1. Gold production and the rise in prices

The rise in prices has become such a long-standing and conspicuous phenomenon that the investigation of its causes occupies economists from the most different tendencies and schools. Among other things, the revolutionising of gold production has been mentioned as one of the causes of the rise in prices. Otto Bauer, in his work on the rise in prices, has accepted this view, and I myself have done the same, at least conditionally. However neither Bauer nor myself, nor, as far as I know, any other socialist theoretician, has considered the reduction in the production cost of gold as the *only* cause of the rise in prices, or even the basic one. In my article on the mass action I identified as causes of the rise in prices:

> [...] the inflationary effects of private property on land in America, which was strengthened by the consequences of the exhaustive cultivation of the soil in Russia and America, by the rise of syndicates of producers and merchants, and *perhaps* also

> the *revolutionising of gold production*. Technical improvements and the finding of new gold mines have perhaps caused the production costs of gold, and with them its value, to fall more rapidly than the value of consumer goods, because as a consequence of the obstructions created by private property on land, the preservation of technically backward small farms, and the migration of agricultural workers, the productivity of agriculture grows slowly. If we add to this the growth of protective tariffs as well as the tax increases of the last years, one has a pretty exhaustive description of the causes of the high cost of living. They are all of a lasting nature. The ruling classes will not give up willingly even the agrarian tariffs and the tax hikes, because they are the necessary consequence of the imperialist colonial and arms fever that has taken possession of capitalism.[106]

Varga, in his recent article on gold production and rise in prices in *Die neue Zeit*, argued against the view that the value of gold has sunk as a consequence of the reduction in its production costs.

He believes not only that the value of gold has actually not fallen, which is perhaps correct, but also that it is impossible that the value of gold could fall. The changes in the conditions of production of gold could not therefore in any case be a cause of the high cost of living. Hilferding accepts this argument and seeks to give it a deeper theoretical foundation in his article on money and commodities.

His theory is bold and apparently very well thought out, but also so paradoxical, that it requires further verification. This investigation must first all cover the theory of paper money, which Hilferding developed in his *Finance capital*, and which he now turns into the foundation of his theory about the unchangeable value of gold.

I pointed out already in my review of Hilferding's *Finance capital* that his theory of paper money seemed to me untenable.[107] [This is what Kautsky wrote there]:

> There is only one point where I cannot follow Hilferding: in his conception that the money commodity (gold or silver) could be replaced by paper not only as a means of circulation, but also as a measure of value. According to him, the real measure of value is not metal money, but the total value of the commodities in circulation (the velocity of circulation remaining the same), which he calls the 'socially necessary circulation value'.

[106] Kautsky 1911b.
[107] Kautsky 1911a, pp. 771–2.

Hilferding probably rejects the opinion that inconvertible paper money as such could be a measure of value. He rightly ridicules Wilhelm Lexis, who defends that opinion in his *Allgemeine Volkswirtschaftslehre*. But he does not improve matters by twisting the relationship between money and commodities, turning the existing mass of commodities into a measure of value, as well as into the creator of value in paper money, in order to make this paper money, thus provided with a certain value, a measure of the values of the commodities. He declares:

> Naturally, commodities are still expressed in money terms or 'measured' in money [not gold!], as they were before the suspension of free coinage. And as before, money continues to serve as a 'measure of value'. But the magnitude of its value is no longer determined by the value of the constituent commodity, gold, silver, or paper. Instead, its 'value' is really determined by the total value of commodities in circulation, assuming the velocity of circulation to be constant. The real measure of value is not money. On the contrary, the 'exchange rate' [*Kurs*] of money is determined by what I would call the socially necessary value in circulation.[108]

This, evidently, can mean nothing more than this: that the real measure of value of the commodities is not money, but on the contrary, the real measure of value of money is the commodities.

If the value of money could be determined in that way by the 'socially necessary circulation value', that would mean the negation of the law of value for the money commodity; it would be saying that the value of the latter is not determined by the socially necessary labour time needed for its own production. The universal applicability of the law of value would be broken through, and that would be all the more astonishing in this case, because it would happen precisely to the money commodity, 'the commodity whose natural form is also the directly social form of realization of human labour in the abstract'.[109]

There is no necessity for that Marxist suicide. The phenomena which appeared during the last decades after the cessation of the free coinage of silver in different countries, and on which Hilferding bases this idea, can be adequately explained in other ways. I will, however, abstain from expressing myself in detail about that. It would involve a

[108]Hilferding 1981, p. 47.
[109]Marx 1976, p. 241.

great expenditure of effort in subtleties, which would perhaps be wasted, as Hilferding's usually very clear method of explanation becomes at times very obscure regarding this particular point, so that I am not always certain of having understood his words in the sense in which he meant them.

But, above all, any long treatise on Hilferding's theory of money is superfluous for the present, because it has no effect in his work, either theoretically or practically.

After he took the trouble, from pages 32 to 56, to construct the pure paper currency, he suddenly came to the following result:

> A pure paper currency of this kind cannot meet the demands imposed on a medium of circulation for any extended period of time. Since its value is determined by the value of the circulating commodities, constantly subject to fluctuations, the value of money would also fluctuate constantly. Money would not be a measure of the value of commodities; on the contrary, its own value would be measured by the current requirements of circulation, that is to say, by the value of commodities, assuming a constant velocity of circulation. A pure paper currency is, therefore, impossible as a permanent institution, because it would subject circulation to constant disturbances.[110]

That is only saying in other words that the replacement of the money commodity as a measure of value by the socially necessary circulation-value is nothing but an academic whim. But, as such, it plays no more part in the course of the book. One can calmly reject it, and yet admit everything that Hilferding goes on to build up on his examination of the different functions of money as means of circulation, measure of value, and means of payment.

It will therefore suffice if, to satisfy my conscience, I simply state my misgivings as to Hilferding's theory of the socially necessary circulation value as a measure of the value of commodities without elaborating upon it.[111]

I thought I had to confine myself to that appraisal and abstain from a detailed refutation, first because my review was already too extensive, and also because I should have had to enter into the details of the theory of money, which most of the readers would easily have mistaken for hair-splitting. One does not deal with a subject like that in a popular journal

[110]Hilferding 1981, pp. 56–7.
[111]Kautsky 1911, Vol. 29, No. 1, pp. 771-772.

without a good reason. There seemed to be no pressing need for a debate on that issue, because paper money plays no role in Hilferding's book, and therefore does not impair its great merits. Hilferding himself declared it to be unrealisable in practice. I therefore felt entitled to consider it as a purely 'academic whim'.

Hilferding's latest article, however, shows that the notions out of which he developed his ideas on paper currency can have greater significance. He made them the basis of an analysis that could have crucial significance for answering the most important economic question of our time—the rise in prices—but that in addition, if it is indeed true, strikes at the heart of our theory of value.

We will now attempt to investigate if that is the case.

2. The paper currency

Let us first of all hear Hilferding himself. He says in his *Finance Capital*:

> Let us first envisage a system of pure paper currency (Herewith is always presupposed government forced currency [*staatlicher Zwangskurs*].). Let us assume that, at a given time, circulation requires 5,000,000 marks for which 3,600 pounds [weight] of gold would be needed. We should then have a total circulation as follows: 5,000,000 marks in C — 5,000,000 marks in M — 5,000,000 marks in C. If paper tokens were substituted for gold, their sum would have to represent the total value of commodities (5,000,000 marks in this case) whatever their nominal value. In other words, if 5,000 equal notes [*Zettel*, slips] were printed, each would be worth 1,000 marks; if 100,000 were printed, each would be worth 50 marks. If the velocity of circulation remained constant and the sum of prices were to double without any corresponding change in the quantity of paper money, the value of the paper would rise to 10,000,000 marks; per contra, if the sum of prices were to decline by one half, the value of the paper would fall to 2,500,000 marks. In other words, under a paper currency [*Papierwährung*] with forced currency [*Zwangskurs*], given a constant velocity of circulation, the value of paper money is determined by the total price of all the commodities in circulation. The value of paper money in such circumstances is completely independent of the value of gold and reflects directly the value of commodities, in accordance with the law that its total amount represents value equal

> to the sum of commodity prices divided by the number of monetary units of equal denomination in circulation. It is obvious that paper money can appreciate as well as depreciate in relation to its original value.[112]

Hilferding then refers to the experiences of different countries in which, with the cessation of free coinage of silver, the value of the silver coins exceeded their metal value, which is supposed to corroborate his views, and finally comes to the following conclusion:

> Money continues to serve as a 'measure of value'. But the magnitude of its value is no longer determined by the value of the constituent commodity, gold, silver, or paper. Instead, its 'value' is really determined by the total value of the commodities in circulation, assuming the velocity of circulation to be constant. The real measure of value is not money. On the contrary, the 'exchange rate' [*Kurs*] of money is determined by what I would call the socially necessary circulation value. If we also take account of the fact that money is a medium of circulation ... this socially necessary circulation value can be expressed in the formula:
> $\frac{\text{total value of commodities}}{\text{velocity of circulation of money}}$
> plus the sum of payments falling due minus the payments which cancel each other out, minus finally the number of turnovers in which the same piece of money functions alternately as a means of circulation and as a means of payment.[113]

Let us look more closely into those remarks. The first sentence already contains the seeds of a misunderstanding. He says:

> Let us assume that, at a given time, circulation requires 5,000,000 marks for which 3600 pounds of gold would be needed.[114]

According to this idea one could suppose that 5 million marks and 3,600 pounds of gold are two different things. Gold would be the means for bringing 5 million marks into circulation. Actually 5 million marks are nothing but 3,600 pounds of gold. The former is identical with the latter, and can be nothing else. What the circulation required were the 3,600 pounds of

[112]Hilferding 1981, p. 39. [*Zwangskurs* was given as 'legal-tender' in the existing translation.]
[113]Hilferding 1981, pp. 47-8.
[114]Hilferding 1981, p. 39.

gold. The fact that people call 1/1395 pounds of gold a mark, and that 3,600 pounds of gold are called 5 million marks, is circumstantial.
Hilferding's sentence is not yet false, but carries the seed of potentially mistaken views.
The following sentence is more significant:

> We should then have a total circulation as follows: 5,000,000 marks in C — 5,000,000 marks in M —5,000,000 marks in C.[115]

Marx employed the formula C—M—C to denote the circulation of commodities. The commodity producer comes to the market with a commodity C, which represents a certain amount of value.
He sells it, exchanging it against a certain amount of bullion M, which has the same value as commodity C, and buys with that amount of money other commodities of the same value, which is why Marx called that commodity also C, although as use value it represents something completely different from the first commodity.
It is clear that C does not represent in Marx's formula a determined amount of money, but of commodities. Had he wanted to denote C concretely, he would have written down a certain weight or number of commodities, such as 40 pounds of coffee, 2 meters of fabric or half a ton of iron. It would not have occurred to him to denote 5 million marks with C. Five million marks denote, as we know, only a certain amount of a particular commodity, gold, measured by weight. It would be senseless to say that in the circulation of commodities, for instance, 1,360 pounds of gold in coffee are exchanged against 1,360 pounds of gold in gold, and again against 1,360 pounds of gold in iron.
Even more problematic, however, is the following thing. C—M—C is the formula for the circulation of *individual* commodities. What Hilferding wants to represent by it, however, is not the *circulation* of *individual commodities* but the circulation of the entire mass of money and commodities in society. But that is the result of numerous circulation processes, which are intertwined in the most diverse ways, and which cannot be collectively represented by the formula C—M—C. In that formula, the value of C must be always equal to M. In contrast, the total value of the money in circulation is almost never equal to the total value of the commodities in circulation.
Hilferding knows all that as well as I do. A few lines later he mentions Marx's formula for the amount of money in circulation. When, despite that, he employs the formula (5 million in) C

[115]Ibid.

—(5 million in) M—(5 million in) C, that is apparently just a mistake, which could be overlooked if it were not the foundation for further errors.
Hilferding continues:

> If gold were replaced by paper signs, their sum would have to represent the sum value of commodities (5,000,000 marks in this case) whatever is printed on them.[116]

This is the first serious mistake resulting from his inexact manner of expression. It is already striking the confusing manner of expression, which is uncommon in Hilferding.
'Whatever is printed on them.' Why does he not express himself more clearly? What can then be printed on the paper signs? Surely not quotations from the German classics, like in modern toilet paper? Only one thing can be printed on them which matters here: how much *gold* they represent. On each note is always printed *which weight in gold* it represents. Let us not forget that.
No less confusing than the expression 'whatever is printed on these signs' is the following one: 'their sum would have to represent the sum value of commodities.' The sum of notes? But they cannot represent any value. It is not a question of the sum of *notes*, but of the sum of *gold quantities* that they represent. Hilferding is clearly attempting, by means of clumsy and vague phrases, to detach paper [currency] from its connection with gold.
And now he takes nonchalantly the decisive step by claiming with the greatest calm, as a self-understood thing, that 'their sum [of paper notes] would have to represent *the sum value of the commodities*, thus in our case be equal to 5 million mark.'
'If gold were replaced by paper signs', paper would still serve as a representation of gold, a determined quantity of gold, not as a representation of commodities. The sum of value that the total amount of notes represents must always be equal to the sum of gold that they replace. In Hilferding's example this sum is admittedly equal to the sum of values of commodities in circulation. Still, that does not mean that their sum also represents the sum value of commodities there, where the former deviates from the sum value of gold required for commodity circulation.
If gold were replaced by paper signs, these would designate certain quantities of gold, not commodity values. They designate M, not C. Whatever quantity of gold they may nominally depict, they can in reality represent no more gold than is required by the needs of circulation.
Now Hilferding will retort, that all this is pure pedantry. The quantity of gold that is required

[116]Ibid.

by the needs of commodity circulation depends on the sum of values of the commodities thrown into circulation. The larger this sum, the greater will be the quantity of gold required. All other circumstances being equal, both stand at a fixed ratio to each other.
Marx himself says in *Capital*:

> On this supposition then, the quantity of the medium of circulation is determined by the sum of the prices that have to be realised.[117]

Does not what Hilferding said amount to the same things?
Not at all, because Marx said that his proposition is true under certain circumstances. The purpose of Hilferding's argumentation is precisely to remove this premise.
'This premise' Marx formulates as follows:

> Henceforth we shall consider the value of gold to be given, as, in fact, it is momentarily whenever we estimate the price of a commodity.[118]

In contrast, Hilferding wants to demonstrate that the value of paper money is independent of the value of gold, and that the total value that paper money represents is determined *directly, immediately* by the value of the mass of commodities confronting it (with the same velocity of circulation).
According to Marx, the value of paper money admittedly is determined likewise by the value of the mass of commodities confronting it, but this process is mediated in Marx's analysis by gold, which, although it is replaced bodily by paper currency, still functions as before as a measure of value, that is as represented gold.
The opposition between the conceptions of Marx and Hilferding emerges clearly in this footnote to *Finance Capital*:

> It seems to me that Marx formulates the law of paper currency (or any currency of restricted coinage) most correctly when he says: "Worthless tokens become tokens of value only when they represent gold within the process of circulation, and they can represent it only to the amount of gold which would circulate as coin, an amount which depends on the value of gold if the exchange-value of the commodities and the

[117]Marx 1976, p. 133.
[118]Marx 1976, pp. 133-4.

> velocity of their metamorphoses are given".[119] *The detour by which Marx proceeds* – first determining the value of the quantity of coins and then, from that, the value of the paper money – *seems superfluous*. The purely social character of that determination is far more clearly expressed when the value of paper money is derived directly from the social circulation value. The fact that, historically, paper currency had its origin in metal currency is not a reason for degrading it in this way theoretically. The value of paper money must be deducible without reference to metallic money.[120]

Here the contradiction between Marx and Hilferding becomes clear. Hilferding thinks that the value of paper currency must be derived from the value of the commodities, with no connection to gold. 'Must' is a hard nut to crack, but in science there is no *sic volo, sic jubeo*.[121] There only *ratio* decides. And there Hilferding's attempt to get rid of gold is not very convincing. He wants to disconnect gold from the determination of the value of paper money, and determine the latter directly through the value of commodities. But, without noticing it, he only succeeds in doing that by implicitly presupposing the measurement of the value of commodities by gold – in other words, by equating value and price. His entire deduction is built on the presupposition that so many marks are not a determination of price but of value. But Marx did not dispute that the value of paper money in circulation is determined by the *sum of prices* of commodities. The way from value to price is precisely the 'detour' that Marx adopted. Hilferding spares himself that 'superfluous' detour by regarding price and value as identical concepts. This error leads him to argue that 5 million marks and 3,600 pounds of gold are different things, and to replace the formula C—M—C for the formula (5 million marks in C) — (5 million marks in M) — (5 million marks in C).

Marx says: Under the presupposition of a given value of gold, the mass of means of circulation is determined by the sum of prices of commodities to be realised. Hilferding, in contrast, declares that the sum of money signs 'must always represent the sum of value of the commodities, and therefore in our case must be equal to 5 million marks.' Those 5 million marks are not a sum of values, but of prices. Value is determined by the socially necessary labour time. If a socially necessary labour time of 5 million hours of work goes into the production of a given mass of commodities, its value will be accordingly high. If an hour of

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[119]Marx 1987, pp. 352–3.
[120]Hilferding 1981, p. 383.
[121][The first part of the sentence is a German proverb: *Muss ist eine harte Nuss*. The last part is a quotation from Juvenal, Satire VI (against women), line 223. The full saying is *Sic volo, sic iubeo; sit pro ratione voluntas*: 'This I will, this I command: let [my] will takes reason's place'.]

labour produces 1/1395 pounds of gold, and if one calls that amount of gold a mark, one can also say that the sum of value of the mass of commodities amounts to 5 million marks. Strictly speaking, however, this is not a sum of values but of prices, that is, a determined magnitude of values, expressed by a certain quantity of gold, against which it is exchanged. Value and price are by no means the same thing, although to simplify matters one can sometimes in theory equate one with the other. But therewith one must not forget, that the expression of the value of a commodity in money presupposes the value of the latter, and that it is senseless without this presupposition. It is always more accurate to call such an expression price.

Why does then Hilferding talk about a sum of values rather than a sum of prices? The sum of value of commodities is given; it is independent from the value of gold. The sum of prices, by contrast, presupposes not only a certain value of commodities, but also a certain value of gold. Equating the sum of values to the sum of prices enables Hilferding to make the price as well as the value of commodities appear independent from the presupposition of a given value of money.

This equation of value and price is the basis of Hilferding's theory. He continues:

> If 5,000 equal notes were printed, each would be worth 1,000 marks; if 100,000 were printed, each would be worth 50 marks. If the velocity of circulation remained constant and *the sum of prices* of commodities were to double without any corresponding change in the quantity of paper money, the value of the paper would rise to 10,000,000 marks [*so werden sie 10 Millionen Mark gelten*]; per contra, if the sum of prices were to decline by one half, the value of the paper would fall to 2,500,000 marks.[122]

Here apparently every connection between money and gold has disappeared. We have on one side a mass of commodities, and on the other a mass of paper notes. The magnitude of value [*Wertgröße*] of the paper notes depends on the value of the mass of commodities and on the amount of paper notes. Gold seems to have been totally eliminated.

And yet, despite everything, the importunate metal intrudes again and again also into this nice paper economy.

What do we have according to Hilferding's presupposition? A mass of values, a heap of commodities representing perhaps 5 million working hours, and an amount of 'identically

[122]Hilferding 1981, p. 39.

printed' notes. The paper notes are in themselves valueless; they acquire their value through the monopoly that the state accords them for the circulation of commodities. The value of each note is determined by the value of the commodities that it has to circulate. If only 5,000 notes are available, each one accounts for 1,000 working hours. If 100,000 notes are thrown into circulation, each represents 70 working hours.
In that form paper currency would be nothing but an inferior copy of the utopia of 'labour-money'. On the latter Marx said:

> The question: why does not money directly represent labour-time, so that a piece of paper may represent, for instance, X hours' labour? is at bottom the same as the question: why, given the production of commodities, must products take the form of commodities? This is evident, since their taking the form of commodities implies their differentiation into commodities and money. Or, why cannot private labour – labour for the account of private individuals – be treated as its opposite, immediate social labour?[123]

Hilferding avoids answering that unpleasant question by presenting the magnitude of value [*Wertgröße*] in marks rather than in working hours. But he may twist and turn as much as he wants: a mark means a certain amount of gold.
As soon as gold is introduced, the whole thing once again makes sense. Hilferding assumes a value of commodities of 5 million marks. That is a definite amount of represented gold; if we understand by a mark 1/1395 pounds of gold, it means approximately 3,600 pounds of gold. Let us assume that for the circulation of that amount of commodities an equal amount of gold is required: we have then 3,600 pounds of gold, but in all their corporeality. If those 3,600 pounds of gold are replaced by notes representing them, their total sum will amount to 3,600 pounds of gold, whatever their quantity. Each note will be printed with the explanation, that it is equal to a certain amount of gold. That is the meaning of the explanation that it is worth 50 or 100 or 1,000 marks. It does not have and cannot have any other meaning. If more notes were thrown into circulation than required by the circulation needs, there would be more representations of gold than the amount of gold that would circulate in their place, and they would be therefore worth only as much gold as required by the circulation process. If it requires 5 million gold marks and there is an amount of paper money representing 10 million gold marks, each note will be worth half its nominal value,

[123]Marx 1976, p. 188, note 1.

and it will buy no more commodities than that.

Otherwise it is impossible to understand the phrase: 'If 5,000 equal notes were printed, each would be worth 1,000 marks; if 100,000 were printed, each would be worth 50 marks'. What mark can here be understood but a gold mark? Besides the paper marks (or mark notes of 50, 100 and 1,000) there are only gold marks, or at least marks in represented gold. Now, a paper mark is always worth a paper mark. The statement that 100 paper marks are worth 50 marks can only mean that they are worth 50 gold marks.

If more paper money were thrown into circulation than required by the needs of circulation of gold money, then under forced currency [*Zwangskurs*] there form double prices: gold prices and paper prices. Gold always remains the basis of value measurement; it cannot be eliminated as a measure of value.

Hilferding denies that. He arrives at this law:

> In other words, under a system of pure legal-tender [*Zwangskurs*] paper currency, given a constant velocity of circulation, the value of paper money is determined by the total price of all the commodities in circulation. The value of paper money in such circumstances is completely *independent of the value* of gold and reflects directly the value of commodities.[124]

The value of money would accordingly be determined by the sum of commodity prices. But how will the sum of commodity prices be determined? Apparently by means of the value of money. It is impossible to say that a commodity is worth 10 marks before I know what value those 10 marks represent. According to Hilferding the value of money with paper currency is determined by the value of commodities compared to the value of money. He fell into this neat vicious circle because he confused value and price. So could the appearance emerge, that commodities have not only a certain value before they are confronted with money, but also a certain price, that is to say a certain exchange ratio with money, whose value is however still totally unknown. If that were true, then the value of money could really originate in the value of commodities and money would 'directly reflect the value of commodities'.

Hilferding does not explain the crucial question: how can commodities get a price before determining the value of money? Without answering it, he reaches the conclusion that with restricted currency the value of money as a measure of value is not determined by the value

[124]Hilferding 1981, p. 39.

of the money commodity but by what he calls the 'socially necessary circulation value', which is given by the formula: (total value of commodities) / (velocity of money circulation) = total value of money (irrespective of payments, which we do not want to include here in order to avoid unnecessary complications).
The formula is constructed in imitation of Marx's formula, which reads:

> The quantity of money functioning as the circulating medium is equal to the sum of the prices of the commodities divided by the number of moves made by coins of the same denomination.[125]

Both formulas outwardly say the same, yet they are fundamentally different.
Marx starts from the sum of prices of commodities, that is to say their sum of value, expressed in a certain amount of coins, for instance marks. Let us suppose that the sum of prices of the commodities turned over daily in a market amounts to 5 million marks. That number must be divided by the average number of daily moves of coins of the same denomination. Since the sum of prices of commodities is assessed in marks, we are considering here only marks, because it is irrelevant how many particular one-mark coins, twenty-mark coins, and so on circulate. If each one-mark coin changes hands five times a day through purchase and sale, a million mark coins will be required to accomplish those transactions.
But in Marx the value of money, the value of a mark, is presupposed as given. What changes with the sum of prices of the commodities and the velocity of circulation of money is not the value of particular coins, but the number of coins in circulation at the same time.
All this is clear and simple. In contrast, in Hilferding's formula we have, as already remarked, the sum of values of commodities, which must be transformed into their sum of prices even before the value of money is determined. But in order to determine the value of the sum of money, and with it the value of the particular coins, we must take into consideration the velocity of circulation of money, which is determined by the number of purchases accomplished within a certain period. That is to say, according to Hilferding's formula money must first function as a measure of value and then as a means of circulation, before its value becomes determined [*festgestellt*]—the value that makes it a measure of value and a means of circulation. First the seller determines the price of his commodities. Then they are sold against this determined quantity of money, and only then emerges, as a

[125]Marx 1976, p. 216.

result of these transactions, what the value of the individual money piece is! The value of money, that must be determined before the circulation of commodities (that is to say the exchange of commodities and money) can begin, is made the result of this exchange!

If I understand Hilferding correctly in this, and I do not see how his theory can be understood otherwise, then it is certainly quite astonishing.

But not however entirely incomprehensible. It was not made out of thin air, but represents an attempt to explain certain phenomena about which the theorists of money have belaboured for decades. Those phenomena are close to Hilferding, because the experiences which his fatherland had with the gold currency played a prominent role among them. A theory of the determination of the value of money by the socially necessary circulation value, the complete independence of the value of money from the value of gold, is a genuinely Austrian theory. Since the 1870s the value of silver has fallen very rapidly. That created severe disturbances in the currencies of all the states that had not adopted the gold currency. Among those countries where silver currency still prevailed were Austria and India. Both countries sought relief in the discontinuation of free silver coinage. They limited the number of silver coins in circulation to a certain mass. The result in both cases was that the price of the silver coins was detached from its metal value and rose above it. Hilferding explains that by arguing that the amount of silver money available at the given metal value was not enough for the needs of commodity circulation. He argues that when the sum of commodities required 700 million silver florins, and there were only 600 million in circulation, a silver florin was worth 7/6 of its silver value.

For Hilferding this proves that the value of money with restricted currency is not determined by the intrinsic value of money, but by the socially necessary circulation value.

The fact to which he refers is undeniable. By abolishing the free coinage of silver it was indeed possible to raise the rate of exchange of the silver coins above their metal value.

But under what circumstances did that happen? It happened at a time when the adoption of *gold currency* was inevitable. The trade of the countries with a silver currency with those with a gold currency grew in the course of economic development. Next to silver, gold became increasingly important for the former countries as well. The situation became more and more intolerable for them as the previously pretty constant ratio between the value of gold and the value of silver was upset by the constant fall of the latter. It became indispensable to confront that situation and that is why the free coinage of silver was abolished.

Hilferding says for instance about the suspension of free silver coinage in India:

> The object was to raise the rupee exchange to 16 pence. Under free coinage this rate corresponded to a silver price of about 43.05 pence. In other words, at that price, the silver content of the rupee, if melted down and sold, would have fetched a price of 16 pence on the London (world) market.[126]

When the mints were closed for private coinage, the silver price was 38 pence; the rate of the rupee was 147/8 pence. After silver coinage was discontinued in 1893, it finally succeeded in bringing the price of the rupee up to 16 pence in 1897, while the silver value it contained was merely 8.87 pence.

Now, pence are English money, gold money. The rate of exchange of the Indian rupee is its price expressed in *gold*. Therefore one cannot say that silver money, any more than paper money, is 'completely independent from the value of gold and a direct reflection of the value of commodities'. It is independent from its own metal value, but only because silver as a measure of value was displaced by another precious metal. It was therefore a question of fixing the ratio between Indian silver money and English gold money, which they sought to accomplish by limiting the amount of Indian silver money in circulation to a certain mass. This measure, however, would have occurred to nobody, and would indeed have been impossible, had silver money been the *only money*. It became possible and desirable because *gold* increasingly pushed silver back, especially as measure of value, leaving silver to function merely as means of circulation, and basically confining it to the role of *token coins*. But token coins function merely as means of circulation, not as measure of value. The value of the silver token coins stood above their metal value, but nobody would affirm that, because of that, money does not need to have an intrinsic value, and that this intrinsic value does not determine commodity prices and with them the amount of money required for the circulation of commodities. To be sure silver money did not become completely a token coin with the discontinuation of free coinage. But this discontinuation was only the first step for Austria and India to go over to gold currency. In both countries gold is the legal measure of value.

The experiences with the restricted silver currency therefore do not at all show that the value of money as measure of value is determined by the socially necessary circulation value rather than by its own value, which as a metal it has like any other commodity. In order to be able to prove it, those experiences should have lasted longer without causing serious disturbances in

[126]Hilferding 1981, p. 39.

the circulation of those countries where the restricted metal was the only measure of value. As long as there is no example of a longer-lasting restricted gold currency, I do not feel compelled to revise the analysis of gold as a measure of value developed by Marx in *Capital*, where he wrote:

> Although the money that performs the functions of a measure of value is only ideal money, price depends entirely upon the *actual substance that is money*.[127]

Marx poked fun on the representatives of the 'absurd' quantity theory, 'that commodities are without a price, and money without a value, when they first enter into circulation, and that, once in the circulation, an aliquot part of the medley of commodities is exchanged for an aliquot part of the heap of precious metals'.[128] Hilferding repeats that opinion, but is it not suitable to his theory about the socially necessary circulation value? Also in his theory money enters into circulation without a value. To be sure, he lets commodities enter into circulation with a value, but he is only able to do that by calling their value price.
Finally Hilferding himself becomes uneasy about his theory and therefore remarks:

> A pure paper currency of this kind cannot meet the demands imposed on a medium of circulation for any extended period of time. Since its value is determined by the value of the circulating commodities, constantly subject to fluctuations, the value of money would also fluctuate constantly. Money would not be a measure of the value of commodities; on the contrary, its own value would be measured by the current requirements of circulation, that is to say, by the value of commodities, assuming a constant velocity of circulation. A pure paper currency is, therefore, impossible as a permanent institution, because it would subject circulation to constant disturbances.[129]

In other words: the socially necessary circulation value, when closely looked at, is nothing but a socially harmful, constant disturbance to circulation. Let us therefore rather remain with Marx's 'detour'.

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[127]Marx 1976, p. 216.
[128]Marx 1976, p. 220.
[129]Hilferding 1981, p. 57.

3. The value of gold and the central banks

In his article on money and commodities, Hilferding applies the law of socially necessary circulation value advanced by him to gold currency, after having applied it in *Finance Capital* only to restricted and paper currency.

He claims that under the gold standard that law determines the value of the sum of money employed for circulation purposes.

According to Hilferding, the sum of money employed for circulation purposes is today regulated by the central banks, which absorb all the gold for sale. 'The demand is therefore unlimited.' This gold disappears in the central bank's vaults and is distributed from there to the extent required by the changing circulation value.

Let us suppose that the circulation value grows from 1,000 to 1,500. If there were no gold hoard, the exchange ratio of the gold coins would have to change. 1 mark would now be worth 1½ marks and vice versa.

But thanks to the gold treasure [of the central bank], there will always be as much gold available as required by the circulation value. The central bank will absorb superfluous gold or add gold to circulation if it is lacking.

A change in the value ratio (between money and commodities) cannot therefore develop at all, because for the changes in the value of gold to manifest themselves, money must remain in circulation. Only when commodities and means of circulation face each other directly can they determine each other's value. Money out of circulation – as hoard in the central bank's vaults – stands in no relationship to the sum of commodities in circulation.

> The actual sequence is therefore this. The producer of gold receives 1 kilogram of gold coins for 1 kilogram of gold. The new gold lies in the central bank's vaults. If circulation needs increase, gold flows from the vaults into circulation. Thus the rate of exchange between gold coins and commodities always remains as it was at the beginning of the process. (Hilferding, "Money and Commodities").

In other words, the law of value is abolished for gold as money. Though that might sound amazing at first sight, Hilferding does not find it surprising.

> The law of value requires total economic freedom for its operation, but this freedom is modified for the rate of exchange between money and commodities by the operation

> of the central banks. The specific nature of money makes it difficult to offer an illustrative example, but let us imagine the following situation: in a completely closed, autarchic economy the state introduces a monopoly of oil trade. Let us say that it keeps a reserve of 100 million litres. It sells oil at a price of 30 marks every 100 litres to everyone, and is always ready to buy back the oil it sold at a price of 29½ marks. The result would naturally be a constant oil price of 30 marks. This price would decide what other oil fields would be exploited, which oil fields would yield rents and how high those rents would be. A growing demand for oil would be met from the reserve, and the 'policy of the oil bank' would always be to secure an adequate quantity. If the demand decreases or production is especially abundant, the reserve also increases, which would be considered an especially favourable circumstance by the bank clerks. The sequence of events with gold is entirely analogous, only that in this case the invariable exchange relation can with compelling certainty be proved only theoretically. (Hilferding, "Money and Commodities").

[According to Hilferding,] the central banks are today a sort of gold monopoly. Formerly gold had 'no unlimited demand', today by contrast the central banks absorb all the gold and besides at a fixed price.

The decisive thing is the fixation of the coins as a certain weight in gold, and the absorption of all the gold by the central banks at this fixed 'gold price'.

Then again 'the central bank is committed, and it could not be otherwise, to satisfy immediately the needs of circulation as soon as they arise'. (Hilferding, "Money and Commodities").

In this way a 'social regulation of circulation' was established through the central banks, [a regulation] which did not exist as long as gold, coming from private mines, was bought by private persons, who also accumulated the gold hoards. Under those circumstances, the value of money was indeed determined by its production costs. Today it is determined by the ratio between the amount of money in circulation and the socially necessary circulation value, and since that ratio is always kept at the same level by the central banks, we have a constant gold value. The production conditions of gold may change as much as they want, but the value of gold remains always the same.

Hilferding triumphantly reaches this conclusion:

> This is then the effect of the 'unlimited demand' for gold [in countries with a gold

> currency]. It brings about the *stabilisation of the exchange relation of gold coin* and *therewith* of gold bullion, as long as the continuous conversion of gold into coins is guaranteed by law. But with this we also have actually had, ever since the general introduction of the modern gold currency systems, a *fixed measure of value*, which the economists looked for so long but which they still did not recognise, when they already had it for a long time. (Hilferding, "Money and Commodities").

I regret having to stay even today, after this clarification, among the ranks of those economists.

First of all, the example of the state monopoly of oil trade must be disposed of. If a state attempts, according to Hilferding's example, to introduce a monopoly of the oil trade, the result would be not a constant oil price, but the bankruptcy of the state, no matter whether it is a closed commercial state or not. Let us suppose, in analogy with the contemporary development of gold production, which we are trying to explain, that the conditions of production of gold change, partly as a result of the discovery of new, richer fields, partly through technological improvements in its extraction. A vast mass of oil becomes available, but consumption does not change. The retail price remains the same and does not change, as [the constant] consumption would require it. The state does not sell more oil than it formerly did, but it is pledged to buy at the old price all the newly-offered oil. Hilferding thinks that this would increase the reserve. He also believes that the bank clerks would consider that 'an especially favourable circumstance', though he does not explain why. It is clear that the state will finally run short of money to buy new oil, if it constantly buys more than it sells. The monopoly of the oil trade can be introduced, with constant prices, only when the state itself owns all the oils fields, and production can be maintained always at a certain level. But if the monopoly remains a purely commercial monopoly, as the analogy with gold production requires, the state must have the possibility of reducing the price when production, and with it supply, exceeds a certain level. Hilferding says:

> The sequence of events with gold is entirely analogous, only that in this case the invariable exchange relation [between money and commodities] can with compelling certainty be proved only theoretically. (Hilferding, "Money and Commodities").

Now, with the 'completely analogous conditions' of the oil monopoly one can demonstrate with 'greater certainty' the *impossibility* of a 'constant relation of exchange' [between money

and commodities].
Hilferding would perhaps object that his remarks must be taken with a pinch of salt. The analogy between gold and oil would apply if there were an unlimited supply of oil. Then its price could always be kept at the same level, whatever the production conditions. But now the central banks have developed an unlimited demand for gold.
What does that unlimited demand for gold consist of? One must not understand by it, for instance, that everybody needs gold and nobody has too much of it. That is an old story, even if it remains always new. According to Hilferding, the unlimited demand exists since the creation of the central banks, that absorb unlimitedly all the gold brought to the market. How does that happen?

> At first this only means that for 1 kilogram of gold always 1 kilogram in gold coins will be given. This *new kilogram* initially disappears in the vaults of the central bank and is stored there as *treasure*. (Hilferding, “Money and Commodities”).

If Hilferding handed over a ten-mark note and received a gold krone, he should not think that he received 'new gold' that he can deposit as 'treasure'. His 'treasure' remains exactly as it was before, only its form has changed.
The same happens with the central bank when it absorbs gold. It gives for 1 kilogram of gold ingots 1 kilogram of gold coins and owns after this transaction not a single penny more gold than it did before. It can let the gold ingots be minted again, and then exchange once again the coins for ingots, and then repeat this process indefinitely. But since when is that an 'unlimited demand for gold'? That 'demand' is nothing but the unlimited willingness of the central bank to *exchange* all the gold that comes to it against another money form. Nobody will want to argue that the money exchangers generate an 'unlimited demand' for the money that they exchange.
However, not all the gold has to be exchanged against coins. The gold can actually increase the central bank’s hoard and disappear in its vaults, if it is not exchanged against coins but against paper money, that is against a money instruction [*Geldanweisung*]. In that case a new amount of gold is added to the one already existing [in the central bank’s vaults]. Through this process all the gold that comes into the market can be absorbed. Does perhaps the unlimited demand for gold consist in that?
New gold comes into the central bank’s vaults. But it does not belong to it. It actually belongs to he who owns the instruction on it. When he presents the instruction, it must be redeemed.

This gold was therefore not acquired by the central bank; it is a deposit of the owner of the money instruction, of the banknote. Here the 'unlimited demand for gold' reveals itself as the willingness of the central bank to store every amount of gold coming into the market. The gold hoard of the central bank is nothing but the union of the gold hoards of the money owners in the country, which was previously split into countless cash boxes and cellars and is now centralised. This centralisation has its advantages, but is only achievable when the central bank accepts every gold hoard that it is asked to take in.

That is the whole secret of the 'unlimited demand for gold' that the central banks allegedly generate. It changes nothing in essence, but just a little in the mechanism of hoarding [treasure-building], which already functioned under developed commodity production before the establishment of those banks. And the same is true of the 'social regulation of circulation' which the central banks supposedly introduce instead of the former anarchy of circulation. Hilferding says:

> Formerly, the entering [of gold] into circulation was not as mechanical a process as it is today. Gold back then had *no unlimited demand*. It had to be exchanged for commodities, and therefore entered immediately into circulation and remained in it, unless private hoarding set in. This hoarding, however, again did not depend on the circulation needs, but on the private capacity of individuals to carry out such hoarding. (Hilferding, “Money and Commodities”).

Why previously gold *had to be* exchanged for commodities by the gold producers immediately after its production is not clearly evident. On the other hand, the gold producer has again today no cause for not immediately exchanging his gold against commodities. Hilferding believes that the central banks absorb the gold and only release it when the needs of circulation require it. But, as we have seen, the gold that the central bank exchanges for coins is not a new hoard. And the gold producer wants the coins in order to put them into circulation, for instance in order to buy means of personal consumption or means of production. He employs his money in the same way, when he exchanges his gold against banknotes or other paper instructions. If he is a capitalist, he does not let his gold lay idle, but buys, for instance, shares from whose proceeds rails and locomotives are bought for Chinese railways. In any case he seeks to put his money into circulation. The establishment of the central banks makes no difference at all. Whether the newly produced gold remains in circulation or is temporarily hoarded never depends on the central bank’s will but on the

needs and wealth of the private money owners – today as in the past.
And the same is true of the 'regulation of circulation' by the inflow of gold [into the central bank]. Hilferding says:

> The central bank hoard (reserves) directly serves as a reserve of circulation; the central bank is committed, and it could not be otherwise, to satisfy immediately the needs of circulation as soon as they arise. The situation was completely different when that regulation did not exist. If from the circulation needs resulted that the gold exchanged for commodities grew in value, there was no reason for private persons to throw money into circulation. (Hilferding, “Money and Commodities”).

How do people throw money into circulation? In no other way than by buying commodities (I am abstracting here, as elsewhere in this work, from the function of money as a means of payment, in order to avoid unnecessarily complicating the analysis). Circulation is always commodity circulation, the buying and selling of commodities.
The buying of commodities by particular persons depends on their needs as consumers and producers. The central bank does not change them in the least. It does not increase the amount of needs. Admittedly, the buying of commodities does not depend on necessities only, but also on the amount of money that we dispose of, as we all sometimes painfully feel. If the amount of money available as hoard is not enough for the purchases required by the household or the business, then one must draw on credit, and try to borrow money from others who have accumulated hoards. Circulation is created by those money expenditures by particular persons.
What does the development of the central banks change? Do they give money to people so that they can buy commodities? Unfortunately that kind of social regulation of circulation does not exist. It is always particular persons who create the circulation through their purchases, either with their own or with borrowed money. The change consists simply in the fact that part of their money lies as deposits in the central bank, which must first release it, and further in the fact that the central bank becomes their first credit provider. Only in that way, through money advances and credits to particular physical or juridical persons, does the central bank throw money into circulation. In point of fact, it does not at all throw money in circulation - except inasmuch as the central bank buys commodities itself. It is the private persons that throw into circulation the money borrowed from the central bank, according to their needs and their means.

The modern method of putting money into circulation differs only in *form* from the method used before the advent of central banking, but not in *essence*. As previously, we have no social regulation of commodity circulation, and therefore also no regulation of the circulation of money, which is determined by commodity circulation. Like before commodity circulation is effectuated by the needs and means of private persons. The central bank can, thanks to its huge machinery and greater insight into the circumstances of private persons, overcome more easily many circulation stoppages and grant credit more suitably and quickly than many isolated money capitalists could possibly do. But the circulation process of commodities is only a part of the entire production process; it is therefore determined by the needs and results of the production process, and as long as private property in the means of production holds good for the process as a whole, a social regulation of part of it is out of the question, even in a metaphorical sense. Of course Hilferding did not mean to use his proposition about social regulation in a literal sense.

But no matter what may be understood by social regulation, the establishment of the central banks by no means changed the essence of the circulation of commodities and money, as Hilferding believes.

The unlimited capacity of society to absorb gold – the 'unlimited demand for the latter' – is not a discovery of the central banks; it has existed ever since there was commodity production, because gold became the commodity regarded as the social material expression of wealth, and gained the form of direct general convertibility. That is why it became money. A commodity that people will not receive gladly at any time and in any quantity cannot become money. And the hoarding of gold is just as little a discovery of the central banks. Reading Hilferding's comments, one might get the impression that money hoards were first regularly accumulated in the central banks, and that, before them, accumulation was a matter of chance, left to the arbitrary will of particular persons, which might just as well not have happened. An actually uninterrupted, regular commodity production is almost impossible without the accumulation of sums of money at different times and places, from which the owners again throw money into circulation according to their needs. The lack of such money pools would not, as Hilferding argues, change 'the exchange rate of the gold coins [with the commodities]' owing to the law of circulation value; it would rather make the continuation of commodity circulation and commodity production impossible.

Hilferding writes:

> the central bank also accepts every redundant gold piece in circulation and adds it to

> its reserve; a change in the value ratio [between money and commodities] cannot therefore develop at all. (Hilferding, “Money and Commodities”).

The situation is different when no gold hoard exists [in the central bank]:

> Let us suppose that the circulation value grows from 1,000 to 1,500. If there were no gold reserve, the exchange rate of the gold coins would have to change; 1 mark would be now worth 1½ mark, and vice versa. (Hilferding, “Money and Commodities”).

In other words: if the circulation value drops from 1,000 to 1,500, each mark will be worth 50 pfennigs if there is no central bank to absorb the superfluous gold coins. That is the real meaning of 'vice versa'.
Such a situation is naturally completely unimaginable, because if coins of twenty marks containing 20/1,395 pounds of gold were worth only 10/1,395 pounds of gold, everybody would transform them into full-valued gold by melting the undervalued coins. But generally speaking, did not a situation ever arise where more gold money circulated than was required by the needs of circulation? Was then anyone forced by the lack of a central bank to spend all the money that he has? What he did not need for the purchase of commodities, and hence for commodity circulation, he kept in his pocket, if there was no central bank in whose vaults he could deposit it in.
Hilferding’s formula for the circulation value, as we have already seen, was built upon the model of the law that Marx advanced for determining the amount of money in circulation, which reads:

> The quantity of money functioning as the circulating medium is equal to the sum of the prices of the commodities divided by the number of moves made by coins of the same denomination.[130]

'This law holds generally' says Marx. It is not some sort of ideal that was first realised by the central banks. For Hilferding however the law only applies since the establishment of the central banks, and under those conditions no changes can take place in the value of gold.

> For changes in the value of gold to manifest themselves, gold must remain in

[130]Marx 1976, p. 216.

> circulation. Only when commodities and means of circulation face each other *directly* can they mutually determine their values. (Hilferding, "Money and Commodities").

What is this again but the 'hypothesis that commodities are without a price, and money without a value, when they first enter into circulation, and that, once in the circulation, an aliquot part of the medley of commodities is exchanged for an aliquot part of the heap of precious metals'?[131] The only difference between the vulgar quantity theory and Hilferding's theory of circulation value is that the former includes in the heap of precious metals all the extracted gold (or silver) available at a given moment, while Hilferding understands by this heap only a part of the gold, found in circulation, which in his view can always be kept by the central banks in a certain ratio with the medley of commodities. Provided that the heap of precious metals maintains always the same ratio vis-à-vis the medley of commodities, increasing and decreasing in the same way, then the same aliquot part of the medley of commodities will always be exchanged for the same aliquot part of the heap of precious metals. That train of thought lies at the basis of Hilferding's statement:

> If circulation needs increase, gold flows from the bank's vaults into circulation. *Thus the rate of exchange between gold coins and commodities always remains as it was at the beginning of the process*. (Hilferding, "Money and Commodities").

However, Hilferding proves here more than he wanted to prove. He wanted to show that under those circumstances the value of gold remains the same. But the rate of exchange between gold coins and commodities is not the value of gold, but the *price of commodities*. If Hilferding were right, *then commodity prices would remain unchanging*.

Here the basic error of his whole theory of circulation value becomes evident. It leaves aside completely the fact that commodities are furnished with prices, and that they have therefore measured their value with gold before entering into circulation. In order for gold to accomplish that function as a measure of value it just has to be imagined [visualised], but it must previously have a certain value. Whether the actual gold circulates or remains in the central bank's vaults or in the stocking of a peasant's wife, does not concern in the least its function as a measure of value. Commodities come to the market provided with prices, and therefore as representatives of a certain amount of gold. How much gold is required to buy all the commodities depends on their sum of prices as well as on the velocity with which the

[131] Marx 1976, p. 220.

different purchases and sales follow each other and the money changes hands. It is not the amount of money in circulation that determines the 'exchange rate between gold coins and commodities', that is to say the sum of prices of the commodities, but on the contrary, it is the sum of prices of the commodities that determines the amount of money in circulation – a sum of prices, which presupposes the values of the commodities as well as the value of gold. Hilferding believes that if always as much gold is in circulation as required by the circulation needs, the rate of exchange between gold coins and commodities remains unchanging. But one of the factors that determine the circulation needs is precisely the rate of exchange between gold and commodities.

Just as little as Hilferding's remarks in *Finance Capital* does his article on money and commodities give cause for revising the view developed by Marx in *Capital*, according to which gold enters into circulation with its own value, which is ultimately determined by the socially necessary labour time, and commodities enter into circulation with certain prices, thereby determining the amount of gold required to accomplish their sales. I do not see the slightest reason for assuming that anything changes therein when the central banks centralise the function of hoarding and control the distribution of money from those hoards. Hilferding's theoretical comments, despite their ingenuity, are wrong because at their origin value and price were not sufficiently kept apart. But with purely logical deductions, just as with mathematical calculations, an insignificant error at the beginning suffices to falsify all further logical consequences and calculations, and to bring them increasingly into contradiction with the correct result the further they are carried forward, no matter how correct and faultless they may be in themselves. The brilliance of the thinker only serves in this case to make the mistake more difficult to recognise.

Finally, the conclusion of Hilferding's analysis, if he were right, would be that the advent of the central banks resulted in the immutability of commodity prices. But even if we understand Hilferding's 'value relation' [*Wertverhältnis*] [between money and commodities] or 'exchange relation [*Austauschverhältnis*] of gold' [with commodities] not as commodity prices, but as gold value, we come no less into contradiction with the facts. Because it is certain that the value of bullion, gold no less than silver, has changed at different times in the course of developed commodity production. Not only did a great revolution in the conditions of production of the money market take place in the seventeenth century. As recently as a few decades ago a similar revolution took place in the production of silver, and its natural consequence was a definite fall in the value of silver, even in countries with a silver standard. And there were already then central banks with great metal hoards

that received in their vaults every silver penny withdrawn from circulation.

Neither practical experiences nor theoretical considerations give us any plausible ground for accepting Hilferding's theory about the determination of the value of money by the socially necessary circulation value, and for assuming that the law of the determination of value by socially necessary labour is abolished by the appearance of the central banks precisely for 'the commodity whose natural form is also the directly social form of realization of human labour in the abstract'.[132] On the contrary, the fact that even such a sharp thinker and solid student of our mode of production as Hilferding failed as soon as he departed from that theory of value is a new proof of its correctness – for gold as well as for any other commodity.

[132]Marx 1976, p. 241.

Chapter Eight

Gold Production and the Rise in Prices[133]

(5 April 1912)

Otto Bauer

In this article, Bauer sides with Kautsky in his controversy against Hilferding, stating tht "the price is not just a simple image of the commodity's value, but a reflection of the commodity's value in the gold's value.' Bauer restates his previous argument that the reduction in the production costs of gold was one of the causes of pre-WWI inflation against both Hilferding and Varga's claims to the contrary, and undertakes to show '*how and by what means* the fall in the value of money brings about the rise in commodity prices.' In Bauer's opinion, Varga had accepted the law that production costs plus the average rate of profit determine the prices of production dogmatically, overlooking the intermediate links between the reduction of production costs and the changes in commodity prices. Actually, the influence of the decreased costs of production of gold on commodity prices takes place, as it does in all cases, through shifts in supply and demand brought about by the redistribution of social capital, which reduce market prices to production prices.

Bauer found Hilferding guilty of a similar overlooking of the intermediate links through which the equalisation of profit rates takes place for gold production, which ultimately affects the exchange rate between gold and commodities. Actually the rise of commodity prices did not derive from '*the ratio between the amount of money in circulation and the [amount of] commodities to be turned over*, but from *the distribution of capital between gold production and commodity production*.' Bauer claimed that this analysis, unlike Hilferding's, took as its starting point production rather than circulation, and that it did not base itself on the quantity theory of money but on the law of the equalisation of the profit rate. This led Bauer to the opposite conclusion from Hilferding: with the reduction in the production costs of gold, commodity prices rise because, 'oOnce the rate of profit increases in gold production over the social average, the newly accumulated surplus value is not fed into commodity production, but into gold production. The total capital of society is distributed differently than before between gold and commodity production, and thus begins that process in which commodity prices rise and through their rise the profit

[133]Bauer 1912.

rate of gold production is reduced back to the average rate of profit.'

Bauer closes with an excellent description of the way in which the bourgeoisie uses inflation to increase exploitation, linking the fight against the high cost of living with the fight for socialism: 'The greed for increasing exploitation is inherent in capitalism. The old means of satisfying them fail because of the resistance of the working class. The capitalists can no longer prolong the working time, or cut wages, but through the rise in prices they reach the same goal by other means. Commodity prices rise faster than wages, thus altering the distribution of the social value-product to the detriment of the working class. The formation of relative surplus value no longer takes place through cuts in money wages but through the rise of commodity prices [and the fall in real wages]. One of the many means for that purpose is the expansion of the gold industry. The working class has no way to prevent this expansion. It can only fend off its effects by abolishing commodity production, stripping gold of its money character, and making the distribution of social labour and social labour income, which is now mediated by money, the immediate task of organised society itself.'

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If the value of gold sinks, commodity prices increase. This proposition has been denied by comrades Varga and Hilferding. If their reasons are true, then we must revise our views on important issues of monetary, price and wage theory.

Kautsky already destroyed the theoretical basis of Hilferding's proposition with sweeping arguments. But Kautsky still left unperformed one task: namely, *to reveal the social mechanism through which the price law asserts itself*. It will therefore be our task to show *how and by what means* the fall in the value of money brings about the rise in commodity prices.

We consider the influence of gold production on commodity prices in a developed capitalist economy. Under this assumption, competition is dominated by the tendency to the *equalisation of profit rates*. The law of value does not apply directly but is mediated by production prices. Just like commodities against each other, money is not exchanged for commodities in proportion to their *values*, but in proportion to their *prices of production*, that is in such a way that in gold mining, as in every branch of commodity production, an equal share of the social surplus value is allotted to equal capitals. We have to show now how this law asserts itself.

For this purpose, we shall at first disregard gold production and recall how the adjustment of prices to changes in production costs takes place *within commodity production itself*. We know that shoes will be cheaper if we manage to reduce their production costs. But how does this happen? What changes are brought about in the whole body of the national economy by the reduction of production costs in a single branch of production? If we first understand what economic processes are triggered by the reduction of production costs in any branch of commodity production, then we will understand more quickly and easily what changes cause gold mining operations.

Production costs and prices in commodity production

Let us compare industry and agriculture. We assume a capitalistically-operated agriculture, and moreover in its most developed form: the leasehold system. Let us assume that the profit rate in industry and agriculture is 15 per cent. The ground rent falls to the landlords' share as rent.

Now let us assume that production costs in industry are reduced by 10 per cent by the introduction of machines. If the market prices of industrial products remain unchanged, then the rate of profit in industry will rise to 27.7 per cent. By contrast, let us assume that production costs in agriculture have remained unchanged; the profit rate of agriculture will thus continue to be 15 per cent.

Now competition immediately begins to equalise profit rates. To this effect operates: 1. the competition within industry itself, 2. the competition of industry with agriculture over the newly-formed capitals.

First, let us examine the competition within industry itself. The manufacturers that first introduced the new machines sell their goods more cheaply in order to beat their competitors. As a result, the prices of industrial products are reduced. We assume they are pushed down to such an extent that the rate of profit in industry is reduced from 27.7 per cent to 21 per cent. Then it is still 6 per cent higher than the profit rate in agriculture.

The competition between industry and agriculture over the newly-formed capital is determined by this disparity. Only a portion of the surplus value that flows each year to the capitalist class is consumed, the other part is accumulated. The capital newly-formed through accumulation is distributed among the various branches of production. Which part of this newly-formed capital will fall to the share of industry and which part to agriculture?

We assume that agriculture had so far had at its disposal 30 per cent of the social capital, that industry commanded 40 per cent and that the remainder had been available to other branches of production, such as trade and so on. But now that the rate of profit in industry is much higher than in agriculture, the former will attract the newly-formed capital more strongly than the latter. Some tenants will not renew their leases and will transfer their capital to industry. Others will buy industrial shares, instead of perfecting the farms. The banks will put their capital at the disposal of industry rather than agriculture. Industrial shares will be sold more easily than mortgage bonds. So industry will expand faster than agriculture. The share of industry in social capital will increase from 40 to 45 per cent, while the share of agriculture will decrease from 30 to 25 per cent. The result is that the reduction of production costs in industry will *change the distribution of capital among the different branches of production*.

The productive forces of industry have now been significantly expanded. The supply of industrial products grows faster than demand. The price of industrial products declines. The profit rate [in industry] falls from 21 to 16 per cent.

The development of agriculture has been inhibited by the rapid expansion of industry, which absorbed the newly-formed capital and the population growth of the working class. Agriculture developed more slowly than it would have done if the increased profit rate of industry had not deprived it of capital and labour. The supply of agricultural products has grown more slowly than demand. The prices of agricultural products increase. The rate of profit [in agriculture] increases from 15 to 16 per cent.

The reduction in the production costs of industry had *reduced the prices of industrial products* even lower than their *values*; on the other hand, *the prices of agricultural products* have increased, although their *values* have remained unchanged. Only in this way can the equalisation of profit rates take place. Of course, the rise and fall of prices is limited by the law of value: despite the rise here, the sinking there, for the whole society the sum of prices remains equal to the sum of values.

Now the equality of profit rates is restored: in agriculture as in industry, the rate of profit amounts to 16 per cent. We have assumed that at the end of the process the profit rate is one per cent higher than at the beginning. In reality, it depends on many circumstances whether the equalisation of profit rates takes place at a higher, unchanged or reduced level.

The introduction of new machinery in industry made workers redundant. They increase the industrial reserve army. The pressure of surplus labour power lowers wages. In the fall of wages expresses itself the fact that, through the reduction in the cost of the industrial

products necessary for the reproduction of labour power, the value of labour power was reduced. The technological revolution of industry here means the creation of relative surplus value. The rate of surplus value rises, and therefore also the rate of profit.

However, it may happen that labour organisations are strong enough to prevent the fall in wages. The wages remain unchanged, although the reproduction costs of labour power have decreased. The newly-created relative surplus value does not accrue to the capitalist class, but to the working class. Wages have risen above the value of labour power. In this case, the rate of profit [in industry] does not increase.

On the other hand, the shift of capital from agriculture to industry means an advance to a higher organic composition of capital as a whole. The constant capital of society grows faster than the variable capital. The rate of profit therefore decreases, unless the rate of surplus value has risen so fast that, the higher organic composition of capital notwithstanding, a higher rate of profit can be achieved.

Finally, agriculture supplies the main raw materials of industry. The rise in the prices of raw materials means an increase in constant capital, a further transition to a higher organic composition, and therefore again a [downward] pressure on the profit rate.

Whether the rate of profit at the end of the process is higher or lower than at its beginning, depends on whether and to what extent wages fall, whether and to what extent the organic composition of capital in industry is higher than in agriculture, whether and to what extent the raw materials for industry were made more expensive by the backwardness of agriculture. But in any case, the equalisation of profit rates is the result of the whole process.

We can now graphically illustrate the whole process in the following table.

Industry	**Agriculture**
40 per cent of the total capital	30 per cent of the total capital
Profit rate 15 per cent	Profit rate 15 per cent
Reduction of production costs	Unchanged production costs
Tougher competition	Unchanged competition
Prices fall	Prices remain unchanged
Profit rate 21 per cent	Profit rate 15 per cent
Increase of the share of total capital to 45 per cent	*Reduction of the share of total capital* to 25 per cent
Accelerated increase in supply [of industrial products]	Slower increase in supply [of agricultural products]
Prices fall	*Prices rise*

Profit rate 16 per cent	Profit rate 16 per cent

The process shown schematically in this table has really taken place in the last decade. It is undoubtedly one of the main causes of the rise in prices that the growth of agricultural production in the world economy has lagged behind the growth of industry.[134] The rapid technological development of industry has not only *reduced* the prices of industrial products, but also deprived agriculture of the capital and labour that would otherwise have flown to it, thereby finally *raising* the prices of agricultural products.

However, many industrial products have become more expensive because the reduction in their production costs was more than offset by the rising prices of the agricultural raw materials supplied to them by agriculture. Thus fabrics, despite the improved machinery of the spinning and weaving mills, have become more expensive, because the production of sheep's wool and cotton was unable to keep pace with the development of industry, so that the prices of sheep's wool and cotton have grown. The *value of the product* of industry has increased, although its *value-product* has fallen.[135]

But we are only interested here in establishing the fact that the reduction of production costs in one branch of production not only *lowers* the prices of its products, but also *increases* the prices of the products of all the other branches. That this happens under certain conditions has already been noticed by Ricardo and Marx in a particular case.[136] For our investigation of the influence of gold production on commodity prices this finding is of great importance.

Our study has thus yielded the following results:

1. The reduction of production costs in some branches of social production changes the distribution of capital among the various branches of production.

2. Thus the ratio between supply and demand will change in the commodity market. The rise of supply in the industry whose production costs have been reduced will be accelerated, while it will be slowed down in all other industries.

3. As a result, the price of the commodity whose production costs were reduced decreases, but at the same time grow the prices of all other goods.

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[134]See Bauer 1910, pp. 13–8.

[135]Product value and value product: see Marx 1978, p. 453. ['Smith's first error, then, is to equate the *value of the annual product* [*jährlichen Produktenwert*] with the annual *value product* [*jährlichen Wertprodukt*]. The latter is simply the product of the current year's labour; the former includes, on top of this, all those elements of value that were used in the production of this annual product, *but which were produced in the previous year and partly in still earlier years*: means of production whose value only *re-appears* – and which, as far as their value is concerned, have been neither produced nor reproduced by the labour spent during the current year. This confusion enables Adam Smith to juggle away the constant component in the value of the annual product'.]

[136]See Marx 1981, p. 302 and following. – Marx 1989a, pp. 417–8.

These laws apply to all goods. Whether they are also valid for gold, is now to be investigated. In this study, it should be noted that the reduction of market prices to production prices cannot take place other than *through the redistribution of social capital,* which *changes the ratio between supply and demand in the market*.[137]

But already at this point we can correct of comrade Varga's mistakes. Varga believes that my assertion that the reduction of the production costs of gold increases the price of [all other] goods, is based on two different, independent ideas, namely: 1. on the doctrine that production costs 'automatically' determine prices, 2. on the assumption that the expansion of gold production increases the demand for goods and thus brings about an increase in commodity prices. Varga overlooks the fact that the influence of decreased costs of production on commodity prices never takes place otherwise than *through the shifts in supply and demand brought about by the redistribution of social capital*. I do not know of any 'automatic' assertion [of the law that production costs plus the average rate of profit determine the prices of production]. If I want to show that the reduction in the extraction costs of gold increases commodity prices, I can provide proof only by showing the changes between supply and demand on the commodity market caused by the change in production costs in the gold mining industry, which bring about the change in commodity prices. Varga has obviously accepted the law according to which the costs of production determine prices only as a dogma; the *intermediate links* between the reduction of production costs and the changes in commodity prices, which mediate between the former and the latter, seem to be unknown to him.

Gold production and commodity prices

Let us assume that the total production costs in a gold mine amount to 1,000,000 marks. With this expenditure one can extract [an amount of] gold that is exchanged by the central bank for 1,150,000 marks in gold coins, notes or bills of exchange. The individual rate of profit in this gold mine is therefore 15 per cent. The average social profit rate is also 15 per cent.

In addition, there are more efficient gold mines; for instance mines in which, with an

[137]'Capital withdraws from a sphere with a low rate of profit and wends its way to others that yield higher profit. This constant migration, *the distribution of capital between the different spheres* according to where the profit rate is rising and where it is falling, *is what produces a relationship between supply and demand such that the average profit is the same in the various different spheres*, and values are therefore transformed into prices of production' (Marx 1981, p. 297).

expenditure of 1,000,000 marks, a surplus product of more than 150,000 marks is obtained. These mining companies obtain a differential rent. Where the contractor is not also the owner of prospecting rights, the differential rent does not accrue to the former but to the latter. The entrepreneur obtains only to the average profit of 15 per cent.

By contrast, mines with a lower yield cannot be operated, because capital will not be content with lower profits, as long as it can achieve in any other branch of production a rate of profit of 15 per cent.

Let us assume that a new machine is introduced in gold mining. It is now possible to obtain a greater amount of gold at the same cost. With an expenditure of 1,000,000 marks, [an amount of] gold will now be obtained that the central banks will exchange for 1,300,000 mark in gold coins, notes or bills. The rate of profit in gold mining has now risen from 15 to 30 per cent. It is twice as high as the profit rate in all other branches of production. The entrepreneurs in the gold mining pocket an extra profit.

This extra profit now attracts new capital to the gold mining industry. Previously, an expansion of the gold mining industry had never taken place, because all the gold mines that promised to yield a rate of profit of 15 per cent were already in operation, while mines with a lower yield could not be operated. From the masses of surplus value [newly] accumulated each year, therefore, not even a tiny section went into gold mining; it flowed completely into the other branches of production. But now gold mining attracts the newly-formed capitals. Banks make capital available to it; the stock market gladly accepts gold stocks. Newly-formed capitals that would otherwise have gone to the production of commodities now flow to gold production. If previously one per cent of the total social capital was invested in gold mining, the share now rises to two per cent. Therefore *the distribution of social capital among the different branches of production has changed*.

What effect has this change in the distribution of social capital had on the commodity market?

The *demand* for commodities has risen. The country in which gold extraction expanded has an increased demand of production equipment for the mining industry and of food for the workers employed in mining. It appears on the world market as a stronger buyer. But also the shareholders of the gold mining companies who do not live in the gold mining country itself, but in the great centres of the capitalist countries, purchase more goods, because they receive higher dividends. The banks' shareholders in Europe and America also buy more goods, because they were enriched by the founders' profit which was realized through the establishment of gold mining companies and the increase of their share capital. Finally, the

stock exchange speculators also buy more goods, because they have made large spread profits [*Differenzgewinne*] through speculation in gold mining stocks.

What happens now with *supply* in the commodity market? Of course, the product range has increased, because every year a portion of the surplus value is accumulated and added to production, i.e. it is used to expand production, to increase society's wealth of commodities. But the supply of commodities has risen more slowly than it would have done if no new machine had been introduced in gold production. For had no technical progress occurred in gold production, then gold production would not have attracted the slightest particle of the newly-accumulated surplus value, and 100 per cent of the newly-accumulated surplus value would have been employed in the expansion of commodity production. But since technological progress in gold production did take place, perhaps 5 per cent of the newly-formed capitals in the world economy were fed into gold mining, and only 95 per cent were employed in setting up new factories or expanding existing operations in other sectors of production. The supply of commodities thus increased more slowly than it would otherwise have done, had no technical progress in gold mining taken place.

Thus, in the first phase of the process, technical progress in gold production on the one hand *accelerates* the growth of demand on the commodity market, while on the other hand it *slows down* the rise in supply on the commodity market. Therefore, *commodity prices* begin to rise, and with them grows the *rate of profit*.

We have seen earlier that the reduction of production costs in industry lowers the prices of industrial products, but also increases the prices of agricultural products. We see here a similar phenomenon. But with one important difference: there commodity prices had fallen on one side, and had risen on the other. Here, however, commodity prices rise everywhere. Because if, in our previous example, only *the distribution of capital within the production of commodities* had changed, while here *the share of all commodity production in the total capital* is reduced, because the production of money has a taken up a larger share of the total social capital.

The rising demand for commodities, the rise of commodity prices and the higher rate of profit now bring about further effects. Commodity sales go on smoothly and the capitalists benefit from the strong economy. First, they can use their capital better. Since all commodity stocks are sold quickly, the *turnover time of capital* is shortened. The *circulation time* decreases, the share of *production time* on the entire *turnover time* of capital increases.[138] The capitalists are able to expand their production with the same amount of capital; they can

[138]See Marx 1978, p. 200.

employ more workers and process more raw materials. The employment of more workers increases the demand on the labour market; a part of the industrial reserve army is used to service the growing demand for food to feed the masses of workers, hence food prices also rise. The processing of more raw materials increases the demand for industrial raw materials, thus also raising their price. In that way is also improved the economic situation of the industries that produce those foodstuffs and raw materials. There, too, we witness the expansion of production, the increasing demand for the raw materials and food they consume, and the further dissemination of the tendency for all prices to increase.

Now capitalists no longer just seek to exploit their capital better but also try to use new capital in order to expand their production faster. This they manage to do without difficulty; first, because the increased production of gold itself makes possible the *expansion of credit*, and second, because the *mass of accumulated surplus value* has increased.

The expansion of credit takes place because the newly-extracted gold flows to the central banks. The gold reserves of central banks increase, and therefore, *ceteris paribus* [all other things being equal], the rate of interest decreases. A lower rate of interest stimulates individual industries; the *construction industry*, in particular, flourishes only with a low interest rate. The expansion in construction activity increases the demand for building materials and for food for construction workers. Also the *state* and the *municipalities* expand their operations more easily with a low interest rate, thus increasing demand for railway equipment and the like, and strengthening the tendency of commodity prices to rise.

The mass of accumulated surplus value increases because profits have risen in both gold mining and the other branches of production. That part of the surplus value that is accumulated therefore also grows. The total social capital increases rapidly; hence the rapid expansion of the productive apparatus in all branches of production. This means, on the one hand, an increased demand for means of production, and, on the other hand, an increased demand for labour power, the absorption of the industrial reserve army and an increased demand for food for the workers. Once again, we witness a rise of commodity prices.

If commodity prices have risen, wages have remained the same, and the standard of living of the working class has therefore deteriorated. The costs of reproduction of labour power have increased; wages have fallen below the value of labour power. The workers demand wage increases. A portion of the working class can have their demands accepted, because with the expansion of production the industrial reserve army has been absorbed, and the situation on the labour market is favourable to the working class. Wage increases are thus forced through large battles. Due to the increase in wages, industries with a lower organic composition of

capital are more heavily loaded [with higher production costs] than the productive sectors with a higher organic composition. Therefore, a growing part of the newly-formed capital flows to production sectors with a higher organic composition of capital, while a declining part flows to branches of production with lower composition. In the former, the supply of goods rises faster than in the latter. If commodity prices thus rise in general, the prices of the products of those industries in which the organic composition of capital is lower than the social average grow even faster than the other commodity prices. At the same time, the organic composition of capital as a whole increases, due to this redistribution of capital within commodity production.

The general rise of commodity prices has increased the social rate of profit. But it also brought about, on the other hand, phenomena that counteract this increase: commodity prices have risen faster than wages, industries with a higher organic composition of capital receive a larger part of the newly-accumulated surplus value than to the other industries, the organic composition of capital as a whole has therefore increased, pressing down the rate of profit. These phenomena eventually set a limit to the rising rate of profit.

Meanwhile, however, the rate of profit also decreased in the gold mining industry. Above all, production costs have risen in gold mining, because gold mines have to pay more for means of production and labour power due to the general rise in commodity prices. But besides this, gold production has been expanded, thus leading to the exploitation of gold mines whose natural production conditions are less favourable, whose ores are less rich. If the rate of profit rose in the other branches of production as a result of rising commodity prices, it has fallen in gold production due to rising production costs. The development reaches a point where capital in gold mining – after deduction of the differential rent accruing to the owner of exploration rights – no longer gets a higher profit than the same capital in any other branch of production. The equalisation of profit rates is completed. The equilibrium disturbed by the technological revolution is restored. An expansion of the gold mining industry now no longer takes place.

The technical development of gold production had raised the profit rate in the gold mining industry over the average rate of profit. Such inequality cannot stand the competition of capitalists. It leads to a redistribution of capital that equalises the profit rates again, on the one hand, by increasing the rate of profit in commodity production through the rise of commodity prices, and, on the other hand, by reducing the rate of profit in gold production through an increase in its production costs. The outcome of the process is that gold is again exchanged for commodities in proportion to their prices of production: that is, in a way that

allots an equal share of the social surplus value to capitals of equal size in both gold production and commodity production. This equalisation of profit rates was brought about by the increase in commodity prices.

However, the rate of profit is not the same at the end of the process as it was at its beginning. As a rule, the average social profit rate is increased by the reduction of production costs in gold mining industry.

At the beginning of the process, the profit rate had risen in gold mining industry. Therewith, the social rate of profit was also increased; the total social capital was confronted with a larger social mass of profit. The increase [in the social mass of profit] was originally appropriated by the gold capitalists, but since commodity prices increased, the profit rate rose in commodity production and fell in gold production; the increase was therewith distributed equally among all the capitals active in society. The increase in commodity prices meant that the surplus profit obtained in gold production was distributed among all the capitals in such a way that the same [amount of] capital, wherever it is applied, obtains an equal share of this surplus profit.

Thus the profit rate of all capitals increased. But how was society able to apportion to each capital a greater value than before? It can do this because the mass and rate of surplus value have increased. Since all commodity prices have risen, the goods that the working class can buy with their wages represent a smaller amount of social labour than in the past, before the rise of commodity prices. The share of surplus labour in the working day, and of surplus value in the value-product, has thus increased. The rate of surplus value has risen and with it the rate of profit.

To be sure, a portion of the working class was able to obtain wage increases. Where this was the case, as we have seen, these wage increases limited the rise in the profit rate. But the entire working class never manages to achieve full compensation for every rise of commodity prices through wage increases. A large part of the working class is always forced to be satisfied for a long time, despite the higher commodity prices, with the customary wages. The share of the entire working class in the value-product thus drops; hence the growth in the profit rate.

However, the profit rate is determined not only by the rate of surplus value, but also by the organic composition of capital. The latter increases, however, during the process. If the organic composition of capital rises faster than the rate of surplus value, then the profit rate at the end of the process, despite the higher commodity prices, will be lower than at the beginning. For the single capitalist, this is expressed in the fact that the prices of the means of

production he uses rise faster than the prices of his commodities.

But whether the equalisation of the profit rate takes place at an increased, unchanged or reduced level, in every case, at the end of the process, the profit rate of gold production is equalized to the profit rate of commodity production, both of which are reduced to the average social profit rate.

The reader now probably understands comrade Varga's mistake. He says that the effect of technical innovations in gold production is 'that now also those goldfields that had not previously been exploited can be exploited. But in those goldfields production costs are higher, so that '*the production costs of the price-regulating amount of gold produced under the worst conditions remain the same*'. Quite right! Only that Varga, in his excessive zeal to quickly find the *final result* of the economic process, skips all the *intermediate links*! Technical innovation certainly leads to the gold mining industry being expanded until capital comes across pits that do not yield more than the given average rate of profit. This expansion of gold mining industry can only happen because capital that would otherwise have been lured to commodity production is attracted to gold production, because the share of gold production in the total social capital is increased, and because the distribution of the total capital of society is altered. In this way, the relationship between supply and demand in the commodity market is altered and a rise of commodity prices takes place, by means of which the equalisation of profit rates asserts itself. Secondly, the rate of profit itself is modified: the social rate of profit, which determines which gold mines are still exploitable, is at the end of the process different from what it was at the beginning! All these phenomena have escaped Varga's attention.

Varga writes: 'In the production of the commodity gold, there is no competition'. This sentence explains his whole mistake. In fact, two types of competition are distinguished: 1. *competition within a sphere of production*; 2. *the competition between different spheres of production over the capital looking for investment opportunities*. Competition within a sphere of production leads to all the goods in this sphere of production being sold, in spite of their different production costs, at the same market value. The competition between the spheres of production over capital, on the other hand, equalises the different profit rates of the various spheres of production to the average profit rate, and thus the market values to the prices of production.[139] There is of course no competition within the sphere of production of gold. But gold production shares in the competition of all the spheres of production over capital. This competition makes the law of the average rate of profit assert itself also among

[139]See Marx 1989a, pp. 430–1. – Marx 1981, p. 281.

the gold producers, and its effect is that, if the production costs of gold fall, the exchange rate between gold and commodities also changes until profit rates are equalised.

The circulation of money

Hilferding objects to this theory that gold is taken up by the central banks. It lies in their vaults and does not enter circulation. Therefore, it cannot determine the price of commodities. For changes in the value of gold to manifest themselves, gold must remain in circulation. Only when commodities and means of circulation face each other *directly* can they mutually determine their values'. (Hilferding, "Money and commodities")

It is true that gold is hoarded first in the central banks' vaults. However, during the process part of the gold is always taken out of the central banks again, because the expansion of gold production leads, as we have seen, in the later stages of the process to an accelerated expansion of commodity production, to the sale of larger quantities of goods at higher prices, thus also to an increase in the demand for money. Part of the new gold is therefore always very quickly taken out of the central bank's vaults and into circulation. However, this is irrelevant for the new pricing structure. We believe that we are able to prove that *the exchange rate between gold and commodities is completely independent of whether the gold obtained with lower production costs enters into circulation or not*. Let us assume that the newly-extracted gold remains completely in the central bank's vaults, and that no part of it flows away into circulation. This assumption presupposes: 1. that the gold producers, in the transfer of gold bullion to the central bank, do not receive the equivalent in gold coins, but accept bills of exchange [or banknotes] in lieu of payment; 2. that it is possible, by shortening the circulation time and improving the credit system, to turn over the (in the later stages of the process) rapidly growing amount of commodities without increasing the number of cash transactions.

Now how does that process take place? The gold producers send the gold to the central banks, and get the equivalent value in bills of exchange or banknotes. With them they pay for the means of production and labour power, and the bills of exchange and notes that still remain with them after paying for the production costs represent their profit. If the production costs are reduced, then this profit is larger than before. The extra profit that the gold producers get is now embodied in these bills of exchange.

The fact that gold producers get an extra profit now attracts new capital into the gold mining

industry. This, as we have seen, brings about shifts between supply and demand in the commodity market. In the first phase, the demand for goods is increased while the supply of commodities grows more slowly, since the accumulated surplus value is not invested in commodity production, but in gold production. The fact that the newly-extracted gold remains in the central bank's vaults changes nothing, either in the increase in demand – because the gold producers can buy with the bills of exchange or the banknotes in their hands as many goods as with the gold that these bills represent – or in the relative reduction in supply, for the supply of goods is determined only by the amount of commodities produced, which is now reduced in relative terms, because the banks and stock exchanges have invested their available capital in order to expand gold production rather than to expand commodity production. This shift between supply and demand brings about a rise in commodity prices, hence also an increase in the rate of profit in commodity production. The rising rate of profit now leads, as we have shown, to the rapid expansion of the entire production of goods, thus to an increased demand for means of production and labour power, and therefore to a further rise in [commodity] prices. Again, it is immaterial whether the mass of circulating money increases or not. The increased demand for means of production and labour power drives up the prices of those commodities, even if, due to the development of the credit system, the increased quantity of goods is turned over without increasing the amount of money in circulation. Finally, production costs rise in the gold mining industry, and thereby the profit rate of the gold producers is reduced until it is again equalised to the increased profit rate of the commodity producers. This phenomenon also takes place regardless of whether the [gold] producers pay for the more expensive means of production and labour power in cash, with the bills which they received in exchange for their gold from the central bank, or with the bank notes against which they exchanged those bills of exchange. The whole process is therefore independent of whether it takes place at an increased or reduced monetary circulation.

So how did Hilferding come to assume that the reduction of production costs in the gold mining industry could only increase commodity prices if the newly-extracted gold entered into circulation? This error can be explained by his preoccupation with the *quantity theory*. The quantity theory contrasts the amounts of commodities with the amount of money in circulation. Because in a purchase money is equated with commodities, the value of money in circulation must stand in a particular proportion to the value of the amount of commodities to be turned over. Now, instead of concluding from this finding that the excess money no longer required to turn over the given amount of commodities will be taken out of

circulation and thrown into the central bank's vaults, it [the quantity theory of money] assumes that commodity prices are determined by the amount of money in circulation, that the former adapts itself to the latter. This theory is fundamentally wrong and has of course long since been dismissed. But it led Hilferding to assume that an influence of money on commodity prices could not be conceived otherwise than through an increased circulation of money raising commodity prices. [Hilferding believes that] if the newly-extracted gold does not flow into circulation, it cannot determine commodity prices.

Our views are essentially different from the quantity theory. They do not spring from *circulation*, but from *production*. They do not derive the rise of commodity prices from *the ratio between the amount of money in circulation and the [amount of] commodities to be turned over*, but from *the distribution of capital between gold production and commodity production*. They do not base themselves on the *quantity theory*, but on the law of the *equalisation of profit rates*. They therefore do not presuppose an increased monetary circulation [to explain the rise of prices].

In fact, our views stand or fall with the law of the equalisation of profit rates. Since Hilferding does not want to admit that with the reduction in the production costs of gold commodity prices will increase, it is quite logical for him to conclude that the equalisation of profit rates does not take place at all in gold production, and that an *absolute rent* therefore arises in the gold mining industry. This is the right conclusion from a false premise. In fact, the competition between spheres of production over the newly-formed capital does not tolerate any difference in rates of profit. An absolute rent can only emerge from spheres of production whose production cannot be increased with a higher profit rate, that is spheres that cannot attract new capital even at a higher profit rate. That is not, however, the case in gold production. Once the rate of profit increases in gold production over the social average, the newly accumulated surplus value is not fed into commodity production, but into gold production. The total capital of society is distributed differently than before between gold and commodity production, and thus begins that process in which commodity prices rise and through their rise the profit rate of gold production is reduced back to the average rate of profit.

Hilferding noted quite correctly that *at constant value of the monetary unit*, the quantity of money in circulation, including the value of this quantity, is determined by the social circulation value. For the representation of many processes, given a paper currency or a restricted currency, this formulation is indispensable. But the law is valid only at a constant value of gold! If the value of gold sinks, then we need a larger amount of gold to turn over the

same amount of commodities, *ceteris paribus* [all other things being equal].[140] And even if, by perfecting the credit system and shortening the circulation time, we are able to bring about the turnover of commodities with the same amount of money as before, commodity prices will rise anyway. This reflects the fact that the price is not just a simple image of the commodity's value, but a reflection of the commodity's value in the gold's value. With the mirror also changes the mirror image.

The fight against the rise in prices

We cannot determine what influence the changes in gold mining have had on the development of commodity prices in recent years. The path followed by Varga does not lead to that goal. Had we wanted to investigate this, we should have tried to estimate the size of the capitals employed in gold mining and processing, in the industries that produced the means of production for gold extraction, and in the means of transportation that served the gold industry during the last two decades. These are the capitals that have been withdrawn from commodity production, as a consequence of the reduction of production costs in gold mining, to find employment in gold production. That in the world economy such a big part of social labour is not directed to the production of use values but to the production of the measure of exchange values [i.e. of gold] belongs to the *faux frais*, the *incidental operating expenditures* of the capitalist mode of production.[141] We must pay these *faux frais* of capitalism by buying the commodities more expensively. The larger the part of social labour dedicated to gold extraction, the more oppressive the rise in prices is.

This insight cannot hinder the *fight against the protectionists*. Agricultural tariffs were introduced as a protection against falling world market prices. If they ever had a *raison d'être*, they have lost it today, because world agricultural prices themselves have increased as a consequence of the redistribution of the total capital in the world economy – namely due to the growth of gold production at the expense of commodity production and, within commodity production itself, due to the growth of industry at the expense of agriculture –, so that local agriculture no longer needs protection.

But this knowledge will strengthen our struggle against *imperialism*. The thirst for new gold

[140]"The law that, if the speed of circulation of money and the sum total of the commodity prices are given, the amount of the medium of circulation is determined, can also be expressed in the following way: if the exchange values of commodities and the average speed of their metamorphoses are given, then the quantity of gold in circulation depends on its own value' (Marx 1987, p. 341).

[141]Marx 1978, pp. 213–4.

treasures is one of the driving forces of imperialism. The largest colonial war of recent times had the purpose of removing all obstacles to the expansion of gold production. Today the British working class struggles in giant battles against the pressure of the rise in prices, which they helped to bring about through the Boer War itself!

Finally, however, this knowledge should encourage us to fight against the rise in prices, not just as free traders, or as land reformers, or as opponents of the imperialist policy of conquest, but also and above all as *socialists*. Our primary goal is to teach the masses to recognize the facts of the high cost of living; namely, that they will continue to be slaves of gold, as long as they are unable to eradicate the roots of money power.

The greed for increasing exploitation is inherent in capitalism. The old means of satisfying them fail because of the resistance of the working class. The capitalists can no longer prolong the working time, or cut wages, but through the rise in prices they reach the same goal by other means. Commodity prices rise faster than wages, thus altering the distribution of the social value-product to the detriment of the working class. The *formation of relative surplus value* no longer takes place through cuts in money wages but through the rise of commodity prices [and the fall in real wages]. One of the many means for that purpose is the expansion of the gold industry. The working class has no way to prevent this expansion. It can only fend off its effects by abolishing commodity production, stripping gold of its money character, and making the distribution of social labour and social labour income, which is now mediated by money, the immediate task of organised society itself.

Chapter Nine

On the Question of Gold Production and the Rise in Prices (12 July 1912)

Miron Nakhimson[142]

Miron Isaakovich Nakhimson (1880-1938) was born in Lithuania to a family of Jewish extraction. He studied in Germany and Switzerland, and worked as an economist and journalist. In Russia, he was a member of Bund from 1899 to 1921. He published his works both in German and in Russian, under the pseudonyms Nakhamkis, Politikus and particularly Spektator, the pen-name he used for the numerous articles he wrote for *Die neue Zeit*, including essays on credit, inflation and tariffs. During the First World War he lived in Switzerland and was close to the Kautskyist 'centre.' There he published books and brochures on "Imperialism and trade war", "The economic situation of Switzerland in the world war", "Political Economy: A critical-theoretical illumination", etc. Back in Russia, he wrote books on "The world economy before and after the war" (1924-1929), "Currency reform in the West" (1925), "On the question of the 'stabilization of capitalism': A critical study" (1926), "Introduction to the study of the world economy " (1928), "The theory of agrarian crises" (1929), "The main problems of the world economy " (1930), etc. In the Soviet debates, Nakhimson rejected Varga's underconsumptionism and preferred to explain crises in terms of disproportions between spheres of production. In 1938 he became a victim of Stalin's purges and was executed.

In this article, Nakhimson agreed with Varga's contention that changes in gold production could not have been the cause of pre-WWI inflation, because in his opinion the demand for gold constantly outstripped supply. Technological progress in gold mining made possible the exploitation of new mines; it did not, however, lower the price of gold, but rather increased differential mining rent, and, since there was no rise of the rate of profit in gold mining, a strong shift in the allocation of capital to gold mining had not occurred. Consequently, Nakhimson concluded, the conditions in gold mining industry could not have increased the prices of other goods, and the causes of the pre-WWI high cost of living had to be sought elsewhere.

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[142]Nakhimson (Spektator) 1912.

In my view, Varga's statements contain a correct core. Certainly, it is completely wrong to say – and Kautsky has already demonstrated this convincingly – that the demand for gold *always* exceeds supply because the central banks have an inexhaustible lust for gold. The very fact that they pay no remuneration on deposits and that they greatly reduce the rate of interest in depression times shows, conversely, that they by no means always want to keep large gold reserves. But what is not applicable as a general law *is true for the present period of our economic life*. I contend, in contrast to the bourgeois economists who assume that gold production has increased more rapidly than the demand for gold, that, conversely, the present tension in the money market is not solely a consequence of lack of capital and credit contraction, but also a result of *the inadequate means of circulation*. The enormously increased ground and urban land rent and the tremendous expansion of international exchange requires much more means of circulation than the ones available nowadays. Varga has already compared the newly-added amounts of gold with the growth in production of some major commodities.

Varga assumed that the industrial consumption of gold makes up a third of production. According to the latest estimates by the Director of the United States Mint, Roberts,[143] world gold production in the years 1900 to 1910 amounted to 4,037.6 million dollars, of which 958 million, or about one-fourth of the total amount, was consumed by industry. Accordingly, the amount of gold has not increased by 32.4 per cent, as Varga assumes, but by 35.3 per cent. The overall result, however, changes little, since the production of other goods has increased from 31 to 88 per cent. In addition, according to Sauerbeck,[144] commodity prices have increased from 1888-97 to 1911 by around 20 per cent. Similarly, the world's foreign trade has increased from 1900 to 1909 from 92.6 to 132.3 billion,[145] or by 43 per cent. The aforementioned report of the Director of the United States Mint also points out that India, Egypt, Argentina, Brazil, Mexico and Japan have withdrawn from the market huge quantities of gold (about 1 billion dollars), which remained partly in exchange and were partly reinvested. Then, banks have certainly collected huge sums of gold, but the demand for gold in the main industrial countries was even bigger. Thus, the gold holdings in the United States from 1890 to 1910 grew by 702 million dollars; by contrast, the bank advances and discounts grew by approximately 7,700 million dollars and the note circulation by 557

[143]Since I could not get hold of the new report by Roberts, I gathered these figures from the New York correspondence of the *Frankfurter Zeitung* (6 May 1912).
[144]*Journal of the Royal Statistical Society*, 1909 until 1912.
[145]*Statistische Jahrbücher für das Deutsche Reich*.

million.

The sales of metal and the metallic reserves of the Reichsbank were as follows:[146]

	Sales	Metal Stocks
1876	36.6 billion marks	0.5 billion marks
1900	189.1 billion marks	0.8 billion marks
1911	377.5 billion marks	1.1 billion marks

The metal stock has *doubled*, but sales increased *tenfold*! Since 1900, the metal stock has risen only slightly, but sales have doubled in this decade alone.

Also, purchases of foreign bills, which actually constitute the main element of the gold outflow, have increased over this period from 211.7 to 939.4 million, or by 727.7 million, that is a 343 per cent increase.

In short, the demand for gold *constantly* exceeds supply. If this is so, then Varga's assumption must be true, that the gold price is determined by the cost of production *under the most adverse conditions*. The gold price[147] has therefore not only not decreased but *rather increased*, because people have passed over to extract gold with increased production costs. In fact, the average grade of gold ores in recent years has dropped from 35 shillings 6 pence per ton in 1905 to 28 shillings 1 pence in 1911.[148] From this follows that people have gone over to exploit less rich ores. Consequently, a differential rent for the gold mines with more favourable production conditions had to develop, because the production price of gold has risen.

That the production price of gold must have increased is also evident from the fact that not all the other goods have increased in price; rather, some have declined. According to Sauerbeck the prices of sugar, coffee and tea in the years 1899 to 1908 compared to prices from 1888 to 1897 have declined by 27 per cent. How can this be explained? By a more significant technical progress in those branches of production than in the gold mines? That is very unlikely and contradicts all the known facts about the development of the sugar industry, which has only made modest progress.

But even more striking is the reference to the steady decline in silver prices, which went down from 61.0 in the years 1888 to 1897 to 40.6 in the years 1899 to 1908 and 40.4 in 1911. To the extent of our knowledge, no events have occurred which could depress the price of silver below its production cost. To the contrary, with the awakening of the East Asian

[146]Administration report of the Reichsbank for 1911.
[147][Nakhimson means the price of production, see footnote 3 Bauer 1910.]
[148]*Frankfurter Zeitung* of 24 April 1912.

capitalist countries, the demand for silver grew. Silver production has also increased from year to year; from 1895 to 1900 the average annual silver production amounted to 5.15 million pounds, while in 1910 it was 6.77 million. This could not have happened if the market price of silver had fallen below its production cost. It is furthermore also unlikely that technical progress in the silver mining industry was larger than in gold mining. There remains only the assumption that *the price of gold increased*, whereas the silver price has at least not grown accordingly.

But if the price of gold did indeed increase as a result of the transition to less productive gold mines, it must be said that the current inflation rate is in fact much larger than it appears to us in comparison with gold. Otto Bauer believes nevertheless that those changed circumstances in gold production could increase commodity prices, and that this happened because technical development raised the rate of profit in the gold mining industry and thereby deprived of capital the other branches of production.

Bauer's whole argumentation, which is really true for all other goods, misses the mark here. Gold is the measure of all *commodity prices* and, *independently* of the capital movements, the changes in the value of gold must bring about a change in commodity prices. But apart from that, Bauer's assumption is incorrect. Technological progress could only have increases the *mining rent*, not the *rate of profit*, because the demand for gold, as we have pointed out, *constantly outstrips* supply. Every advance in gold mining made possible the exploitation of new mines; it did not, however, lower the price of gold, but rather increased the mining rent. The capitalist entrepreneur was content to remain with the same rate of profit, while the mine owners reaped the surplus. Capital could not therefore prefer gold mining in particular (apart from the fact that the growth in mining rent requires much capital for the acquisition of gold mines, just like the increase in ground rent puts a strain on the capital market) because there was not much more to get there than anywhere else.

Indeed. Let us assume that the capital invested stands in a certain ratio to the value generated in gold mines and in the mining industry. The value of gold production from 1896 to 1910 has increased by about 125 per cent. The value of mining production in Germany grew during this period from 786.7 to 2,008.6 million dollars, or more than 150 per cent; in the United States it increased, from 1896 to 1909, from 640 to 1885. 6 million dollars, or almost three times;[149] in other countries slightly less, but all the same it rose significantly.

[149] *Statistical Abstract for the principal and other countries in each year from 1897 to 1907/08* and *The Statesman's Yearbook*, 1911. According to preliminary figures from the American census the capital invested in American industry increased from 1900 to 1910 by 9.9 to 20 billion dollars, i.e. it doubled, and since 1899 it has tripled.

According to Ruppel[150] in London, in the years 1901 to 1907, the following amounts of capital have been raised for mines (in millions of pounds of *nominal* capital):

	In general	Among it for gold mines
1901	87.5	28.6
1902	140.7	88.1
1903	76.8	82.8
1904	66.5	22.8
1905	86.8	20.0
1906	59.2	18.9
1907	29.4	7.1

This shows that the share of gold mining values in the total capital consumed by the mining industry has declined gradually.

A strong shift in the allocation of capital as a result of technological progress in gold mining has not therefore occurred. Consequently, the conditions in gold mining industry could not affect the prices of other goods. Nevertheless, we conduct our struggle against inflation not only as 'free traders' and 'land reformers'. Bauer himself has shown in his splendid writing that the basic cause of inflation lies in the capitalist mode of production in general and in the anarchy of the distribution of products in particular. Only that the *faux frais*, the 'incidental operating expenditures' of the capitalist mode of production, consist not only in the production cost of gold, but also in the ever-rising cost of distribution. The number of people employed in trade has grown twice as fast as the population, which naturally had to increase the share of the commercial class in the price of goods. We therefore need not unproven hypotheses in order to condemn the current inflation and with it the capitalist mode of production: the established facts condemn capitalism more sharply than any hypothesis.

[150]Ruppel 1909.

Chapter Ten

Gold Production and the Rise in Prices[151]

(17 January 1913)

Eugen Varga

In this article Varga restates his thesis that changes in gold production could not have been the cause of pre-WWI inflation and attempts to prove it by means of statistical data. He argues that, since the capital operating in gold mining amounted to no more than 1.5 per cent of the total capital, the flow of capitals into gold production could not have affected the rate of exchange between money and commodities and therefore could not have been the cause of the rise in prices. The causes of the pre-WWI high cost of living therefore had to be sought elsewhere, in the changing conditions of commodity production—about which, however, Varga provided no further explanation in the current article.

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In his article 'Gold production and the rise in prices', comrade Otto Bauer solves the problem of showing us how the reduction in the production costs of gold translates into the increase in commodity prices by correctly explaining that, although there is no competition within the sphere of gold production, there is a competition between all the spheres of production, including the production of gold, over the newly-accumulated capitals looking for productive investment opportunities. A cheapening of gold production at temporarily constant prices of gold and a constant purchasing power of money means a surplus profit for the capitals invested in the gold mining industry. Investment-seeking capitals therefore eagerly seek out for gold production, while the other industries lack new capital: commodity production does not keep pace with the growing demand, and [commodity] prices necessarily increase.

This method of explanation is, as I already mentioned in my first article, the only theoretically correct one: only in this way is an increase in commodity prices due to the reduction of the production costs of the money material at all possible. But I must continue to insist that the potential price increase that can be brought about by this shift in the distribution of the newly-accumulated capital, due to its flowing into gold production, is a vanishing quantity.

[151][Varga 1913] Note by the editor [Kautsky]: With this article we take up again the discussion, which had to be halted in July of last year in favour of the debate on the disarmament question.

Now comrade Bauer further asserts that a general rise in commodity prices, based on precisely the same causes, must also occur whenever a reduction in production costs takes place in any area of commodity production. Let us suppose that a technical innovation succeeds in reducing the cost of production of silk fabrics, while the demand for silk fabrics momentarily keeps prices at the old level. The result will be an above-average profit rate in silk weaving. The newly-accumulated capitals turn mainly to silk production. The other production spheres have to do without the influx of new capital. An increased demand is created by the workers employed in the silk industry and the capitalists who employ them, while the supply [of commodities] remains the same. Hence the general rise in prices, in exactly the same way as through an increase in gold production. A temporarily general increase in commodity prices due to the flow of the newly-accumulated capitals into that sphere of production where an above-average profit rate was realised is therefore not a special effect of the reduction in the production costs of the money material, but it theoretically occurs whenever an above-average rate of profit is obtained in any sphere of production. And yet, very large savings in production costs have constantly been taking place during the last ten to fifteen years in individual branches of commodity production due to technological innovations. As a consequence, temporarily above-average profits were realised and extensive shifts in capital investments occurred, but it never occurred to anyone – even to comrade Bauer – to regard these shifts as the reason for a temporary or permanent rise in prices. At this point the difference between the effect of competition in commodity production and its effect in gold production becomes clearly evident. The new capitals flowing into silk-weaving come into competition with the existing enterprises, giving rise to an oversupply of silk goods and a fall in prices – assuming an unchanged value of the money material and money. The surplus profit disappears due to the adaptation of the price of production, which becomes cheaper, to the social production price. The tendency toward the equalisation of profit rates asserts itself here in two ways: 1. through a general rise in all other commodity prices, due to the reduced influx of new capitals and the consequently reduced supply; 2. through the competition of the newly-invested capitals within the relevant sphere of production itself.

In gold production, only the first type of equalisation of the profit rate is possible. The second is not possible, because the price of the commodity gold, in terms of gold coins, does not fall as a result of the cheapening of production costs; the surplus profit continues to exist, and the influx of new capitals lasts as long as mining sites [for gold] continue to exist which, given the reduced production costs, yield the average profit rate prevailing in all the other spheres

of production. If all those gold mining sites are already under exploitation, the further influx of capital is impossible, and a further equalisation of the profit rates through the influx of capital into gold production and the consequent increase in prices does not occur.

I think that the clarification of the fact that competition in gold production does not act as internal competition, that among gold producers there is no competition, but that the production costs of the worst yet mineable pits are determined in advance, and that a reduction in the exchange value of gold vis-à-vis the other commodities only takes place in a roundabout way through shifts in capital investments, is the most important outcome of the discussion that took place [in the pages of *Die neue Zeit*].

The clarification of this situation was all the more desirable, because even comrades as Jacob van Gelderen, who writes for *Die neue Zeit*, were not clear about this situation and clung to internal competition within gold production.

The reason why there was such darkness on this point is, I believe, that Marx talks about the value of gold only at the level of simple reproduction, as do the numerous popular expositions of Marx's theory. Let us quote, for example, Kautsky's:

> Let us, however, assume that gold is the measure of values. But the value of gold fluctuates; one day it may happen that twice as much gold as previously will be produced in the same socially-necessary labour-time. In the productivity of tailoring, however, no alteration has taken place. What happens? The price of a coat now amounts to 20 grams of gold. The change in the value of gold therefore expresses itself perceptibly insofar as it functions as the measure of value.[152]

If we have no specific explanation of the manner in which the reduction in the value of gold asserts itself, it stands to reason to envisage this process, by analogy with other commodities, as taking place through internal competition, which in the actual conditions of the capitalist mode of production is incorrect in the case of gold. An internal competition would only take place if any amount of gold could be produced in this reduced labour time. Since that is not the case, the price of gold continues to be the old one, and the result is an increase in the [gold] mining rent.

Let us suppose that gold (in coin form), iron and silk are exchanged in proportion to the socially necessary labour contained in them. This is possible if the organic composition of capital in all three production areas coincides with the average composition of capital, and if

[152]Kautsky 1936.

supply and demand are so much in equilibrium that the three commodities are exchanged according to their production prices. Let us further assume that the value of 1 gram gold = 100 kilograms of iron = 2 yards of silk.

Now a 50 per cent reduction in the production costs of the labour time socially necessary for the production of silk takes place. The products will then, once the equalisation of the profit rates as a result of competition in silk weaving has taken place, be exchanged [in the following proportions]: 1 gram gold = 100 kilograms of iron = 4 yards of silk.

How would, on the other hand, the rate of exchange be set if the costs of production of gold production decrease by 50 per cent?

Because there is no internal competition in gold production, a price reduction of the newly-extracted gold expressed in the gold coins in circulation is impossible, [and] the rate of exchange will be as before: 1 gram gold = 100 — Δ kilogram of iron = 2 — Δ yards of silk. But by Δ I understand the theoretical price increase of all other products resulting from the flow of capitals into gold production, *and I claim that these are real, in the present moment vanishingly small quantities, that a change in the rate of exchange between gold (money) and commodities cannot therefore result from this, and that the current rise in prices therefore cannot also be due to this cause*.

* * *

The crux of the matter is now as follows: was the reduction of commodity production that took place because of the increased flow of capitals into the sphere of gold production enough to bring about a noticeable rise in commodity prices due to the shift in the ratio between supply and demand? If it was incapable of doing that, then no equalisation of profit rates has taken place, and therefore no general rise in the average rate of profit, because the change was also negligible here. Comrade Bauer claims that the path I took does not lead to the desired goal.

> Had we wanted to investigate this (the influence of capital movements), we should have tried to estimate the size of the capitals employed in gold mining and processing, in the industries that produced the means of production for gold extraction, and in the means of transportation that served the gold industry during the last two decades. These are the capitals that have been withdrawn from commodity production, as a consequence of the reduction of production costs in gold mining, to find employment in gold production. (Otto Bauer, “Gold production and the rise in prices”)

It is of course impossible to provide here an accurate estimate. Nevertheless, a proof is

possible. If we construe all the uncertain numbers to our disadvantage and the result nevertheless confirms our assertion, then our argument is valid despite the uncertainty.

Let us, first of all, try to determine how much new capital was invested [in gold mining] in recent years. In order to determine this, we could simply try to identify the new issues [of stock] and the credit capitals of gold mining in recent years. But this way offers little prospect of success, because a large amount of fictitious capital circulates precisely in the gold mining industry. A very large part of the capital invested in the exploitation of a gold mines is founders' profit [*Gründergewinn*], capitalised mining rent: the temporary owner of an extensive mining site hands it over to a mining company only in exchange for a large sum of money;[153] the capital which he receives is not actually invested, in Bauer's sense, in gold production, but goes back into commodity production.

Let us momentarily try to take a detour.

Gold production is a branch of production with a lower-than-average organic composition of capital: this must be admitted by anyone who has read even as little as a description of a gold mine. The innovations in gold production that took place in the last decade have changed nothing in this respect. The main advance was the introduction of the cyanide process, which makes possible the reprocessing of the debris of the crushing mills and requires no large capital investment.

Let us assume, however, that gold production is carried out with an average organic composition of capital. Currently, not even a million workers are employed in gold production in the whole world. But in the area of the capitalist gold transactions currently at least 200 million workers are productively employed. Let us assume that ten years ago only 500,000 were employed in gold production. In that case, a capital movement has taken place in a ratio of 0.5 million to 200 million, or 0.25 per cent, but it is obvious that such a small shift [in the distribution of capital between gold mining and commodity production] can have had no noticeable effect on commodity production.

We get a similar result when we compare the value of gold production with the value of the product of total world production (we use the term value here, although we are actually talking about prices).

The value of total *mining production* (without smelting) in 1897 amounted[154] to 4,118 million marks, in 1906 to 8,051 million marks. Coal accounted for 81.9 per cent of the value, iron ore for 9.5 per cent, *gold and silver ores* for 1.3 per cent.

The value of metallurgical production in 1906 amounted to 7,114 million marks. Of this

[153] See Epstein 1909.

[154] *Handwörterbuch der Staatswissenschaften*, 3. edition, article on mining.

value, pig iron accounted for 59.1 per cent, copper for 13.6 per cent, gold for 12 per cent.
If we compare the ratio of the value of gold production with the values of mining and metallurgical production, we can already see that gold production amounts to no more than 6 to 8 per cent of mining and metallurgical production, and that in consequence even a considerable increase in gold production can deprive all the other branches beyond mining and metallurgical industry only of a vanishingly small amount of capital.
But the outcome of this comparison is very different if we take the entire world production:

<table>
<tr><td colspan="3"></td><td>Million marks</td></tr>
<tr><td colspan="3">Value of mining production in 1911</td><td>10,000</td></tr>
<tr><td colspan="3">Value of cabin production, minus the values transferred from the mining</td><td>3,000</td></tr>
<tr><td colspan="3">The world's crop[155] in 1910-11 (Million quintals)</td><td></td></tr>
<tr><td>wheat</td><td>961</td><td rowspan="5">3,116 à [multiplied by] 14 marks</td><td rowspan="5">43,624</td></tr>
<tr><td>rye</td><td>454</td></tr>
<tr><td>barley</td><td>230</td></tr>
<tr><td>oats</td><td>569</td></tr>
<tr><td>corn</td><td>902</td></tr>
<tr><td>potatoes</td><td>1,470</td><td>à 2 marks</td><td>2,940</td></tr>
<tr><td>wine</td><td>142</td><td>à 20 marks</td><td>2,840</td></tr>
<tr><td>cotton</td><td>19 bales</td><td>à 100 marks</td><td>1,900</td></tr>
<tr><td>coffee</td><td>12 quintals</td><td>à 120 marks</td><td>1,440</td></tr>
<tr><td>tobacco</td><td>10 quintals</td><td>à 100 marks</td><td>1,000</td></tr>
<tr><td colspan="4">To this end, the value of agricultural products not named here (sugar beet, garden plants, feed), calculated low</td></tr>
<tr><td colspan="4">Value of livestock products (meat, hides, milk, wool)</td></tr>
<tr><td colspan="4">Value of forestry products</td></tr>
<tr><td colspan="4">Value of river and sea fishing products</td></tr>
<tr><td colspan="4">Value of the raw products</td></tr>
</table>

To this may be added the increase in value experienced by the raw materials of mining and smelting, and by the agricultural products, through industrial processing. This increase is difficult to estimate. If we compare the number of employees in industry with the mining and agricultural workers of the capitalist countries, we incidentally get a relationship of 1:2. Now

[155]Estimate of the Hungarian ministry of agriculture and Friedrich 1911.

a large number of agricultural products experience only a very small increase in value until their consumption; on the other hand, the annual value-product of an industrial worker is much greater than that of an agricultural worker. Therefore, we will commit no great error if we estimate the annual value-product of the processing industry of the world at 25 million marks. We thus incidentally obtain a value for the annual value production of the capitalist world of approximately *124,000 million marks*. However imprecise the above estimations may be, at least they are more likely to be too low than too high; the order of magnitude of the numbers is therefore absolutely reliable. In contrast, the value of gold production amounted in the year 1910 to *1,910 million marks*, that is, to 1.5 per cent of the value of annual world production. But if today the value of gold production amounts to at most 1.5 per cent of the value of world production, *a shift of this ratio during the last decades* – if it ever took place, that is assuming that the increase in commodity production in terms of percentage has not rather exceeded that of gold production – *could have had no noticeable effect on prices*.

* * *

Finally we can also make an attempt to determine the share of gold production in the newly-accumulated capital. The value of gold production in the entire world in the year 1901 amounted[156] to 1,096 million marks, and in the year 1910 to 1,910 million marks, that is an increase of 814 million marks, or an annual increase of approximately 90 million marks. If we assume that the profit rate in gold production is equal to the average rate of profit and that the means of production were amortised simultaneously with the new investments, an increase in the value of the product of 90 million marks per year corresponds to an average new capital investment of also 90 million marks yearly. We get a similar result when we look at the new issues [of gold mining stock] in the British capital market. It is well-known that in the gold mining industry mainly British capital is invested. The amounts invested were as follows, in pounds sterling:[157]

	1910	1911
Australian mines (not just gold)	562,400	511,100
South African mines	2,595,700	3,984,300
	3,158,100	4,495,400

Or, rounded off in millions of marks, 64 million in 1910, and 90 million in 1911. But Australia and South Africa provide far more than half of the gold production of the world; in the above

[156] *Statistisches Jahrbuch für das Deutsche Reich,* 1911.
[157] *The Economist* of 12 February 1912. Older data I unfortunately could not track down.

figures, the capital investment of the entire mining industry of the areas in question is assumed to have taken place in gold mining. If we nevertheless double these figures, we get a new investment in the gold mining industry of approximately 150 *million* marks a year. By contrast, *The Economist* estimated the total quantity of newly-invested capital in the year 1908 to have been 848 million pounds sterling, that is 16,960 million marks.[158]

The capital newly invested in gold mining thus amounted, according to these estimates, to less than 1 per cent of all the new capital investments. We know well that all new capital investments include a large amount of *fictitious* capital – claims to a future workless share in the labour product of the workers –, but also that the capital invested in gold shares contains very many fictitious shares (capitalised future mining rent), so that the ratio may be approximately the above-mentioned one.

Whether we proceed from the number of workers employed, from the value-product, or from the capital issues, we always come to the conclusion that the capital operating in gold mining as well as the annually newly-created capital is no more than 1 to 1.5 per cent of the total capital. A variation of this ratio, for instance an increase from 1 to 1.5 per cent, is therefore such a small alteration, that the effect of capital shifts on pricing is negligible. The causes of the current rise in prices must therefore not be sought in gold production but rather in commodity production.

[158]Mulhall, *The New Dictionary of Statistics*. 1911. Article on capital.

Chapter Eleven

The Transformations in Gold Production and the Changing Nature of the Rise in Prices[159]

(24 January 1913)

Karl Kautsky

In a contemporary review of Austin Lewis's English version of Kautsky's brochure published in 1914 by Charles H. Kerr, the reviewer commented: 'The translation cannot be recommended as particularly lucid or careful' (*Journal of Political Economy*, Vol. 22, No. 10, December 1914, p. 1026). We have therefore decided to retranslate it in full. In the foreword to the Russian edition, dated 1 August 1918, the Menshevik David Dallin (1889-1962) emphasised the relevance of Kautsky's brochure given the then-current talk about the gold system being 'outlived', somewhat clumsily calling it a study of the gold currency and holding up the prospect of Russia's return to gold.

Kautsky's brochure is divided into four sections. 1. Simple commodity production; 2. The capitalist mode of production; 3. The circulation of money; and 4. The rise in prices and misery. Analytically, Kautsky proceeds like Marx, investigating first the effect of changes in the conditions of production of gold on commodity prices under simple commodity production, and then proceeding to investigate their effect under capitalist commodity production based on the exploitation of wage labour. Kautsky described his methodological procedure as follows: 'In order to achieve results in science, we must depict and investigate actual relations as simply as possible. Once the connections between things are identified under these conditions, it is easier to recognise the more complicated surface relations... That is why, on the one hand, we have assumed that gold is the only money metal, ignoring silver. We have also assumed that all the gold produced was employed as money. Finally... we have assumed that gold was produced under the conditions of generalised simple commodity production.' This research procedure enabled Kautsky to reach the conclusion that the consequence of the discovery of new, richer gold mines was not a growth of differential rent, but the abandonment of the less productive mines and the consequent reduction in the value of gold, which had inflationary effects. (For an essay criticising Kautsky's research method and accusing him of upholding a version

[159]Kautsky 1913

of the quantity theory of money see Berkovsky 1930c.)

Kautsky then proceeded to examine the effect that changes in gold production have on prices under the conditions of generalised capitalist production. He argued that a reduction in the labour time socially necessary for the production of a given amount of gold brought about the development of an epoch of prosperity, and with it of an increase in commodity prices. The alternation of prosperity and depression connected to fluctuations in gold production did not constitute a circuit like the industrial cycle, but was nevertheless of the greatest significance for shaping the crisis cycle, according to Kautsky. If the expansion of gold production ceased or weakened, the upturn periods became shorter and increasingly feebler, the periods of crisis grew longer, and the crisis took on a chronic character. By contrast, in periods of rising gold production crises were not abolished, but the periods of upswing were lengthened while the periods of crisis and depression were shortened—although Kautsky granted that the alternation of prosperity and depression connected to fluctuations in gold production was not necessarily recurrent but rather depended on a series of accidents. In the following section, he argued that the development of the banks (particularly through the introduction of substitutes for gold, such as banknotes, in the different functions of money, and through the credit system) and of the means of transportation heightened the stimulating effect of increased gold production on the capitalist economy and increased commodity prices.

In the final section Kautsky summarized his arguments as follows 'the process by which the law of value operates in the case of gold. The mode of operation is simply this, that given a stable distribution of labour power in the different spheres of production, increased gold production creates increased demand for commodities and consequently causes a rise in prices. Only when the change in prices thus produced is not enough to enforce the law of value for gold, and when its production under capitalist conditions yields an extra profit for a considerable length of time, does the tendency towards the equalisation of the rates of profit manifest itself as a regulating element, which brings more capital and more labour into gold mining until the equality of the profit rate is restored – a law which is somewhat modified by the distinctive lottery character of gold mining, which always tends to keep the rate of profit in this industry below the average.' Kautsky therefore considered undeniable the theoretical possibility, which he tried to prove by means of statistics, that the pre-WWI rise in prices was connected with the increased gold production.

According to Kautsky, the price-raising effects of gold production were enormously increased in the decades before the outbreak of the First World War by the rise of protective tariffs and monopolies (cartels, syndicates, trusts), the development of absolute ground rent in America due to the private appropriation of the land (which increased the prices of agricultural products), and the arms race brought about by imperialism, which increased the fiscal burden, particularly through indirect taxes.

Kautsky concluded that the prospects for capitalism were bleak because 'the number of places capable of surprising by new extraordinary gold discoveries, and of putting bankrupt capitalism on its feet again for a time by means of a new big discovery, becomes always smaller.' The slowdown in the growth of gold production would put an end to pre-war prosperity, but prices would continue to rise due to the other factors mentioned above, which would have a depressing effect on real wages and increase the misery of the working class. The expected period of increasing misery would sharpen the spur of class antagonisms and strengthen the revolutionary drive of the proletariat 'towards the overthrow of the whole capitalist system and the state power which protects it.' But this ostensibly revolutionary perspective was blunted by Kautsky, already well-embarked in a centrist course after his break with Rosa Luxemburg three years earlier, in the final paragraphs, where he set for the working class the concrete goal, not of seizing power, but of conquering 'new positions of power in the state as against the property-owning classes.'

The brochure closes in a self-satisfied tone, arguing that 'the party and the unions have done their duty' and that socialists 'may confidently face the struggles which the new era of capitalism has in store for us.' A year and a half later, the Second International collapsed and the Social Democratic Party of Germany abandoned internationalism by voting in favour of the war credits in the Reichstag, definitely giving up any revolutionary perspective (Haupt 1972).

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1. Simple commodity production

One of the most disputed questions of economic theory at the present time is whether changes in the production of gold are one of the causes of the current rise in prices. It is not a mere academic question, since expectations about the continuance of the rise in prices, as well as over the effects of the means deployed or demanded [to fight] against it, are closely

associated with the point of view adopted as to the reason of the rise in prices.

In our own party this matter is also fervently debated. This discussion, considering the current significance of the question, would have been even more fervent were it not for the fact that a popular presentation of the matter is very difficult. I hope, however, to be able to make the main points generally clear. If the reader, however, in spite of my efforts, meets with difficulties, it will be for the most part at the beginning of the work. The closing chapter is intelligible in itself without knowledge of the matter preceding it.

Comrade Varga published, more than a year ago, an article in *Die neue Zeit* on 'Gold production and the rise in prices' (1911), in which he set forth the view that changes in the production of gold are not accountable for the present rise in prices, and furthermore that such changes would never cause a fall in the value of gold but only a rise of ground rent in gold mining.

He has recently (1913) sought to support this view, which was contested by Otto Bauer, J.V.G. and myself. Whatever one may think about Varga's views, they have in any case presented an important problem which had not been formerly stated. The statement of a new problem, moreover, constitutes a service to science, when, as in this instance, it is not haphazard, but proceeds from a complete knowledge of the subject.

Varga said in his first article:

> In *Capital* itself we find no analysis of how changes in gold production affect price formation.

Otto Bauer undertook to provide such an analysis, taking into consideration the entire modern production process. But the question under consideration is a problem which already appertains to simple, pre-capitalistic, for instance handicraft commodity production, and which therefore must be solvable also on that basis.

Varga admittedly declares the system of banking to be the reason why changes in the conditions of production of gold should not be able to effect changes in the value of gold. Because the central banks absorb all the gold which comes into the world market, no overproduction and therefore no lowering of the value of gold can take place. So it would appear from this as if the problem were a different one under modern capitalist commodity production than under simple commodity production. But in reality the banks play no part in the economic role of gold in connection with this question, as I have already shown in a former article.

Also under simple commodity production, without banks, the tendency [of the market] to

absorb gold, silver or the money metal in general, finds no limits, because it is money, thus a commodity, and moreover the only commodity of which people can never have enough. Already for simple commodity production, Marx said: 'The hoarding drive is boundless in its nature'.[160] The existence of banks was not necessary to develop this boundlessness, and the capitalist method of using hoards does not change the boundless drive to accumulate.

By its very notion already, money is a commodity different from all other commodities, in that it can be used under any circumstances and in any amount. Precisely thereby the money commodity becomes money.

When Varga concludes from this, that changes in the conditions of production of gold cannot bring about changes in the prices of commodities, he proves too much, since such changes have occurred several times in history, and conspicuously so in the sixteenth century, after the discovery of America.

Once this fact is established, the problem is simply to discover in which way the change in the value of gold asserts itself in the market and expresses itself in prices.

In mere commodity exchange, before the existence of money, each of the two commodities to be exchanged, for example a table and a coat, represents equally both supply and demand. The owner of the table offers it to acquire a coat. He only effects an exchange when a tailor appears on the market who offers a coat and wants a table for it.

As soon as one commodity becomes the money commodity, a change takes place. The table, the commodity, represents now only supply. It can constitute no demand. At the other pole of the world of commodities stands money, which only represents demand, not supply.

The size of demand for a commodity depends on the number of owners of money who feel a desire to acquire it at a given price, and on the amount of money which they have. The amount of money on the market at any given time constitutes the maximum possible demand for commodities at that time – we are here investigating simple relations only, and therefore disregard credit. The more money the population has, all the greater, all other conditions being equal, the demand for commodities. The greater this demand, all the higher, all other conditions being equal, will be the commodity prices.

Naturally, the matter cannot be thought of as if on the one side stood the whole mass of money and on the other the whole mass of commodities available, and prices were determined by the ratio between the two; or as if the owners of money and the owners of commodities were two different classes, constantly standing opposite each other.

The former owner of a commodity becomes an owner of money when he has sold his wares.

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[160]Marx 1976, p. 230.

And the demand for commodities which he now able represents will be all the greater, the more commodities he formerly sold, and the greater thus his former supply was. Within the circle of commodity producers nobody can buy unless he has previously sold, and nobody can represent demand without first having represented supply. On the other hand, nobody who has sold a commodity is compelled to immediately expend the money thus set free in the purchase of a new commodity. He can hoard it. Finally, when he has such a hoard, he can also buy a commodity, without having sold one immediately beforehand.

The relation between supply and demand can therefore be exceedingly variable already at the beginning of commodity production, depending upon a whole series of conditions.

A certain degree of expansion of commodity production requires a certain amount of money (gold or silver) for the circulation of commodities (buying and selling) to take place. The further exponsion of commodity production goes hand in hand with a corresponding production of precious metals, which increases their existing stock. At each moment there is a relation between the mass of money, representing demand, and the mass of commodities, representing supply. But this relation, and with it the level of commodity prices, does not depend upon the total amount of available money metal, but upon those numerous circumstances, which cause sometimes a larger and sometimes a smaller part of this mass of money to appear as demand on the market.

There is, however, a point within commodity production which can be totally independent from these conditions; that is, *gold production*. I speak now for the sake of simplicity only about the production of gold. Wherever silver currency exists, this analysis applies also to silver.

If the producer of gold does not sell his product as raw material to industry, but transforms it into money, he is the only producer in the realm of commodity production who enters the market, not with a supply, but with a demand. The demand which he represents is completely independent from the conditions of commodity circulation, insofar as he is the only producer who does not need to sell his product in order to be able to buy commodities. The increase in the production of gold means under all circumstances an increase of demand in the commodity market. And this increase is by no means limited to the extent of the gold producer's additional production. When the gold producer buys commodities with his product, the former owners of those commodities receive money, and are thereby placed in a position to buy commodities themselves, and so on. Additional gold becomes the starting point for and the impetus to an additional circulation of commodities, from which again a new demand for commodities arises. This additional circulation becomes intertwined with

the circulation already existing, influences it, but is also influenced by it. Its velocity is thus to a high degree determined by the same circumstances that determined the old circulation. In whatever form it may fashion itself thereby, in any case the size of the demand, which the additional gold develops in it, is a multiple of the sum of value of that gold itself.

If, for example, the annual gold production is one hundred thousand pounds of gold, 140 million marks, this sum, if entirely transformed into money, will generate an increased demand for commodities to the extent of 700 million marks a year, if the entire circulation of commodities is such that each piece of gold on an average makes five purchases a year. On the other hand, if circulation is so rapid that each piece of gold accomplishes ten purchases, the additional demand will amount to 1,400 million marks. In any event, it will be much higher than the sum of value of the gold produced.

According to what has been said, it is not very difficult to estimate the effects of a change in the conditions of production of gold.

Let us first of all take a society with simple, that is to say, pre-capitalistic, commodity production, such as handicraft for example. Every worker owns his means of production. No one produces for himself, but everyone produces commodities for the market. There are no machines and no industrial reserve army. All the labour forces are at work and distributed through the various branches of production, so that none of these branches can push ahead of the other unless labour leaves other branches to go into it.

This does not mean that the same amount will be produced every year (simple reproduction), or that each year more cannot be produced than in the previous year (enlarged reproduction). An enlargement of production is possible and usually required, even with simple commodity production, to provide for the increased population. But a sudden increase in production is, under the conditions of simple commodity production, impossible. It can only grow steadily and evenly from year to year.

The circulation of commodities follows the rule of the law of value. The product of an hour of labour is bought with gold, for whose production an hour of labour is necessary.

Now let us assume that in such society the productivity of gold production suddenly changes. For example, let us assume that it is possible, by means of a new invention, to double the production of gold in the existing mines with the same expenditure of labour as before; instead of one hundred thousand pounds (140 million marks), 200,000 pounds of gold are now produced annually.

The productivity of labour in the other branches remains the same; therefore the amount of commodities brought to the market does not grow in proportion to the increase in gold

production. The demand for commodities will consequently grow more strongly than the supply. Commodity prices must therefore necessarily rise, even if there is not the slightest change in the distribution of the social labour forces.

How much the prices will rise, however, will not be just determined by the annual increase [*Mehrbetrag*] in gold production. We have seen that the additional demand for commodities, arising from this increased amount of gold, depends on the manifold and varying conditions in commodity circulation.

In the extreme case we have assumed, in which the productivity of gold production has suddenly doubled, there will no doubt develop a strong new demand for commodities, which cannot be satisfied at the old prices. Every commodity coming into the market will immediately find a buyer, which will accelerate the circulation of commodities, but in that way the demand for commodities will also increase to an even larger extent than it would correspond to the increase in the amount of gold.

For all that, the result does not have to be a doubling of the prices of commodities.[161] When this is not the case, then gold production will have a particular power of attraction for the labour forces of society. The gold digger could then buy with the product of an hour's labour more than the product of an hour's labour. He would have to work less hard than the labourers in other sectors in order to live as well, or he could live better with the same expenditure of labour. That would prompt numerous workers in other branches of industry to leave them and take to gold mining. This means, under the given conditions, that the production of commodities would be reduced, and that of gold increased still further. That would increase again the demand for commodities, until workers in the gold mines cannot live any better than those in other branches of labour and gold digging ceases to attract new labour forces, that is, until with the product of one hour of labour the product of another hour of labour can be bought, and the law of value has asserted itself.

A diminution of [production in] industry and agriculture through the excessive attraction of labour into the production of the precious metals with simple commodity production is not a mere theoretical construction, but has been observed many times in history.

In Spain, after the discovery of the rich gold and silver fields of America in the sixteenth century, numerous labour forces flocked to them. A mass of precious metals was thrown upon the Spanish market, and at the same time the industry of the country declined.

The old historian Anderson, in his history of trade, has cited a set of Spanish statistics for the year 1588, according to which there was then in Spain no more than *one million* male adults,

[161][That is, the equilibrium would remain disturbed.]

thus in total nearly *five million* people. As causes of the depopulation and economic decay, he cites the expulsion of the Jews and the Moors, the numerous European wars of Charles V and Philip II, and finally the strong emigration of numerous elements to the American lands. So while the mere increase in the demand for commodities is not enough to restore the equilibrium in the exchange of equal values, disturbed by the alteration in the value of gold, to it is still added the fact, under simple commodity production, of a reduction in commodity supply.

Now, it might seem, and that could perhaps be objected, that already a mere increase in the amount of the money metal must have the effect of increasing demand and with it commodity prices, even if no decrease in the value of gold had occurred.

I have assumed above that the annual production of gold has doubled as a result of an improvement in technique, which allowed half an hour of labour to produce as much gold as formerly took an hour of labour to produce. One might now assume a different case, in which new gold fields are discovered, which are not richer but just as rich as those hitherto existing, and which, with the same expenditure of labour, can produce the same amount of gold as before. In this hypothetical scenario, too, the annual amount of gold produced is doubled, and with it the demand for commodities and their prices are enormously increased, [but] without any change in the value of gold.

That would be correct if gold fields alone, and not men, were required for the production of gold. According to our first presupposition, the production of gold required no more labour power than formerly in order to double the production of gold. According to our current assumption, twice as many men would be necessary. Whence will they come? Simple commodity production has no industrial reserve army. They must be taken from their previous occupations. But what will induce them to take up the production of gold? They will earn no more in their new occupation than in the old ones. Indeed, since the increase in the amount of gold brought about an increase in commodity prices, while the amount of gold which each miner produces remained the same, they would be better off engaging in the production of other commodities than mining gold. There would therefore be not the least inducement for additional labour power to turn towards the production of gold and to increase it.

Nevertheless, new discoveries of gold would lead to an increase in gold production. The conditions of gold production would remain stable only if all gold fields were equally productive. As is well known, that is usually not the case. Some gold fields are enormously rich and yield a large product with little labour, while there are others whose product is

barely enough to maintain the miners. Similar differences would mark both the new and the old gold discoveries. The richest gold fields would surely attract great amounts of labour power. The increased production would raise commodity prices and thereby do away with the possibility of maintaining the exploitation of the poorest among the old gold fields. Their workers could no longer buy the same amount of commodities with the product of their labour, and therefore could no longer sustain themselves.

The result would not be a doubling of the number of workers in gold mining, but a shift in the existing number of workers within the gold mining industry. Only the rich mines would be worked and therefore the same number of workers would now produce an increased amount of gold, whose sum would represent the same value as that of the gold produced the previous year. The value of a given amount of gold, for instance of a pound of gold, or of a specific gold coin, would therefore fall.

Also here we find a mutual adjustment between the value of gold and the prices of commodities, even though the method of adjustment is here different. Both are mutually dependent, and cannot remain independent of each other.

This does not mean, however, that commodity prices always reflect the ratio between the value of commodities and the value of gold. This is naturally not true for single market transactions. But it is also not true, on average, even if we disregard the modification of the law of value by the equalisation of the rates of profit, i.e. if we consider pre-capitalistic commodity production. Marx says of gold:

> Jacob questions whether gold has ever been paid for at its full value. This applies still more to diamonds.[162]

In other words, the prices of commodities expressed in gold are always higher than should correspond to the full value of the gold. Marx has, unfortunately, not told us how this happens.

The under-valuation of gold is caused, in my opinion, because it not only concentrates a great amount of value in a small volume, but the occurrence of such great value is also very erratic, tied to many chance events.

In a diamond or gold district a worker may find a rich diamond or a gold nugget without much seeking; it will then be hailed by the opponents of the Marxist theory of value as a most striking refutation of that theory. The critics forget, however, the many other diamond and

[162]Marx 1976, p. 130.

gold seekers, who have sought the desired treasure vainly, or with trivial success, and whose labour has been repaid poorly, or not at all. But the gold seekers are like the vulgar economists; they see only the nuggets of the one and not the many failures of the others, and hence go off to mines in which, as a whole, they expend much more labour than they get out as value. That means that, as a whole, they content themselves with a poorer standard of living than other occupations would offer them. We are not speaking of wages. It must be remembered that we are still concerned with the period of simple commodity production, in which the worker still works with his own tools and is the master of his product, not yet being a wage worker. In the production of gold this stage lasts a long time. Even in the middle of the nineteenth century the gold miners in California and Australia were independent producers. In the Klondyke they are for the most part so to this very day [1913]. This has been partly the cause and partly the result of the long-standing technical backwardness in gold extraction. The great privations which the mass of miners endure are well-known. Despite this, they are attracted by the prospects of the fabled gold nuggets. It is the same with the production of silver.

Adam Smith, in *The Wealth of Nations*, in the eleventh chapter of the first book, says

> Neither are the profits of the undertakers of silver mines commonly very great in Peru. The same most respectable and well-informed authors acquaint us that when any person undertakes to work a new mine in Peru, he is universally looked upon as a man destined to bankruptcy and ruin, and is upon that account shunned and avoided by everybody. Mining, it seems, is considered there in the same light as here, as a lottery, in which the prizes do not compensate the blanks, though the greatness of some tempts many adventurers to throw away their fortune in such unprosperous projects.[163]

Just as the fact that lottery tickets bearing no interest find a ready market does not abolish the law that all money capitals strive to obtain the same interest rate, [so too] the fact that gold does not exchange with commodities at its full value does not do away with the law of value.

This law not only says that all commodities at a given moment exchange in proportion to the amount of socially necessary labour contained in them, but also that the value of a commodity, and therefore its exchange rate with other commodities, changes with the

[163]Smith 1909, pp. 180–1.

amount of social labour necessary for its production– that is, it rises and falls proportionately with its magnitude.

In this sense, the law of value applies also for those commodities which for one reason or another regularly exchange above or below their real value.

Varga says that improvements in the methods of gold production must result only in an increase in differential rent in gold mining. If, at the present time, in the poorest mines, two pounds of gold can be obtained with the same labour expenditure, let us say one week's labour by a miner, where formerly only one pound of gold was produced, people will now exploit gold mines whose exploitation was formerly unprofitable. A mine, which with a labour expenditure of one week only produced half a pound of gold, will now yield a pound with a similar expenditure and thus be operable. Mines which previously produced only a pound of gold per man weekly and so yielded no differential rent, will now, when they yield two pounds, pay a rent of a pound of gold per man weekly. The least productive mine, with the highest production costs, is, however, [according to Varga] the one which determines the value of gold. This value will therefore not sink, because the least productive mine still produces a pound per man weekly. The socially necessary labour expenditure for the production of gold and therefore its value remains the same.

This method of proof would be unimpeachable, if it were not for the fact that it merely states what it seeks to prove, namely, that commodity prices do not rise despite the increased gold production. Varga says:

> Because of the cheaper working of ores, a kilogramme of gold can now be obtained by the expenditure of a smaller quantity of minted gold. (Varga, "Gold Production and the Rise in Prices", 17 November 1911)

But gold is not produced by means of gold, but through [the expenditure of] human labour. When, as a result of the increased demand due to increased gold production, the prices of commodities rise, the cost of the articles of consumption and of the tools required by the gold miners also rises. It is precisely those commodities which will rise first and to the greatest extent, because the growth in gold production increases first and foremost the demand for them. The more the price of these commodities grows, all the more will the effects of the saving in labour power in gold mining be offset, and the less will it be possible to operate new mines alongside the existing ones.

If Varga's theory were correct, ground rents in the mining of precious metals would have risen, in the course of time, more than in any other kind of land exploitation

[*Bodenausbeutung*]. But Adam Smith declares that in no other sector are ground rents so low, and Marx supports him. He quotes the following extract from Smith's *Wealth of Nations* in his *Theories of Surplus Value*:

> The price, therefore, of the coarse, and still more that of the precious metals at the *most fertile* mines in the world, must necessarily more or less affect their price at every other in it.
> The price of every metal, at every time, therefore, being regulated in some measure by its price at the most fertile mine in the world that is actually wrought, it can, at the greater part of mines, do very little more than pay the expense of working, and can seldom afford a very high rent to the landlord. Rent, accordingly, seems at the greater part of mines to have but a small share in the price of the coarse, and a still smaller in that of the precious metals. Labor and profit make up the greater part of both.
> As the price, both of the precious metals and of the precious stones, is regulated all over the world by their price at the most fertile mine in it, the rent which a mine of either can afford to its proprietor is in proportion, not to its absolute, but to what may be called its relative fertility, or to its superiority over other mines of the same kind. If new mines were discovered, as much superior to those of Potosi as they were superior to those of Europe, the value of silver might be so much degraded as to render even the mines of Potosi not worth the working.[164]

Ricardo rejects this opinion; Marx, by contrast, agrees with it. However, he noted

> Adam Smith is mistaken when he declares the particular set of circumstances on the market, under which the most fertile mine (or land) dominates the market, to be the *rule*. But provided such a case is assumed his reasoning is correct (on the whole) and Ricardo's wrong.[165]

The 'particular set of circumstances' under which Smith's assumption applies is that development proceeds, not from the exploitation of richer mines to poorer, but on the contrary from poorer to richer ones – i.e. precisely the set of circumstances which is the focus of our investigation.
Therefore, according to Smith and Marx, the consequence of the discovery of new, richer

[164]Smith quoted in Marx 1989a, pp. 570–1.
[165]Marx 1989a, p. 548.

gold and silver mines is not a growth of differential rent, but the abandonment of the less productive mines.

This is not a mere theoretical construction. In the sixteenth century, when the great stream of precious metals, gold and silver, from the newly discovered lands of America, came to Europe, the gold mines in the Alps were shut down. Should we assume that they all became exhausted simultaneously? Or was not rather the rise in prices brought about by the precious metals of America the general reason why the exploitation of all these mines simultaneously turned into a loss-making enterprise?

Ground rent in the gold mines of the Austrian Alps at that time not only did not increase, but rather was entirely destroyed.

Of the silver mines, Smith says in the already much-quoted chapter:

> After the discovery of the mines of Peru the silver mines of Europe were the greater part of them abandoned. The value of silver was so much reduced that their produce could no longer pay the expense of working them or replace with a profit the food, clothes, lodging and other necessaries which were concerned in that operation. This was the case, too, with the mines of Cuba and St. Domingo, and even with the ancient mines of Peru.[166]

Many other things disappeared together with the gold and silver mines in Europe, at least in Germany. There, they had constituted a not insignificant source of strength of Protestantism, in Saxony and Bohemia as in the Alpine countries. The decline in silver mining weakened Saxony, the cradle of Protestantism, and Bohemia, where the Hussite movement had been succeeded by Calvinism. In the Alpine countries it was again due to the discontinuance of gold mining that Protestantism lost its position.

> The decline of mining as a consequence of the competition of the precious metals from America broke the resistance of the miners in the mountains. In the Alpine countries, Tyrol, Salzburg, Styria, etc., mining was almost completely discontinued, and with it disappeared the only progressive-minded element in those regions. The districts which had, in 1525, risen victoriously against the princes and the priests, became the stronghold of clericalism and absolutism; the only districts of contemporary Austria which had taken a vigorous part in the revolution of 1525 became an Austrian Vendée; a transformation, to which in any case the disappearance

[166]Smith 1909, p. 179.

of mining had contributed most.[167]

Thus even religious reform then depended on gold.
One can see how transformations in the production conditions of gold cause also transformations in price relations, in the conditions of production of commodities, and finally even in the power relations between classes.
However, what has been said here applies for the moment only to the conditions of simple commodity production. How do these matters stand in the capitalist mode of production?

2. The capitalist mode of production

In order to achieve results in science, we must depict and investigate actual relations as simply as possible. Once the connections between things are identified under these conditions, it is easier to recognise the more complicated surface relations. If we begin by investigating the latter, we become lost in a labyrinth of 'ifs' and 'buts', and end up with a thicket of question marks.
We must therefore, also in the case under consideration, depict things as simply as possible. That is why, on the one hand, we have assumed that gold is the only money metal, ignoring silver. We have also assumed that all the gold produced was employed as money. Finally, in the previous chapter, we have assumed that gold was produced under the conditions of generalised simple commodity production. Let us now examine the effect that changes in gold production have on prices under the conditions of generalised capitalist production. In reality, however, there are numerous intermediate stages. For example, in the above-mentioned mines in the Alps gold was produced capitalistically by entrepreneurs who

[167]Kautsky 1889, p. 515. Praising this article series as Kautsky's best work so far Engels wrote: 'Your articles on the miners in Thuringia are the best you have done so far—a genuine study that deals exhaustively with the main issues and, moreover, aims simply at investigating the facts and not, as in your paper on population or that on the primaeval family, at confirming a preconceived opinion. That is why you have succeeded in producing something substantial. The work throws light on an important part of German history and, though there may be a few minor gaps in the argument, this is of no real moment. Reading it, I realised clearly for the first time (what I had only dimly and vaguely perceived in Soetbeer) the extent to which gold and silver production in Germany (and Hungary, whence precious metals were distributed throughout the West via Germany) provided the final impulse which, between 1470 and 1530, put Germany in the lead economically in Europe, thereby making her the focal point of the first bourgeois revolution, in the religious guise of the so-called Reformation. The final impulse in the sense that the guild crafts and the commission trade reached a relatively advanced stage of development, thus turning the scales in Germany's favour rather than in that of Italy, France or England' (Engels' letter to Kautsky, 15 September 1889, in Engels 2001, p. 376). See also see the chapter '*Kapital und Arbeit im Bergbau*' in Kautsky 1895. Munro 2003 argues that this earlier Central-European silver-copper mining boom (due to application of technological advances from the 1450s onward) was one of the initial causes of the inflationary 'price revolution'. Later in the sixteenth century there was also the introduction of the patio process in America.

employed wage labourers, in the midst of a society in which simple commodity production was the dominant form, which went hand in hand with an extensive production for self-consumption. In Spanish America, by contrast, the workers in the gold and silver mines were Indian slaves. In California and Australia, again, still half a century ago gold mining was carried out under conditions of simple commodity production by free producers, who owned their own tools and land. But this type of gold production constituted a very essential component of a highly developed capitalist system of production.

We must abstract from these intermediate stages.

Let us therefore assume now capitalist gold production amidst a capitalist society. In this society: what effects would a change in the conditions of production of gold have—let us say, a reduction in the socially necessary amount of labour required for the production of a given quantity of gold? Since we are concerned here with the question of the rise in prices, we only have to take into consideration the consequences of a reduction, and we can leave out of consideration the consequences of an increase in the amount of labour required for the production of gold, that is, of a decline in the productivity of gold mines.

The gold mines are owned by the capitalists. So also the facilities and machinery necessary to work them and extract the gold. The workers are wage workers. They are paid like other hired workers. The question of the productivity of labour is thus immaterial to them. If the production of a pound of gold formerly took two working weeks of one man, but now only takes one, this does not mean that his weekly pay will be doubled. It remains for the moment the same, so long as the increased gold production does not change the price of the necessaries of life. The extra pound of gold which the two working weeks now produce does not imply increased production costs. It is pure profit for the capitalist who owns and works the mine.

This condition, however, cannot long continue. Now will be annually added to the existing gold stock twice as much gold as previously, which, at unchanged prices, will bring about an increased demand for commodities.

The consequences for the commodity market are now, at the beginning at least, identical with those under simple commodity production. The additional gold admittedly is no longer spent by the gold digger, but by his exploiter. The latter may use the increased amount of gold in the most different ways. He can buy articles of consumption or means of production to increase his business. But he can also loan it directly or indirectly in the form of the purchase of interest-bearing government securities or obligations, or acquire shares in other businesses, stocks.

The more capitalism develops, all the more will these last forms of expenditure of newly-acquired gold be employed. And it is especially in these last forms that gold leaves the possession of the gold producers to spread over the world.

Thereby a remarkable phenomenon is explained, to which the Director of the United States Mint alludes in his report for the year 1911, a report which contains a wealth of important material on the gold question.[168] That phenomenon is the fact that the majority of the mines in the world belong to England, and yet only a minimum of the gold extracted from them flows to England. From December 1899 to December 1910, there flew to the large banks of Europe 863 million dollars in gold (some 3½ billion marks), of which, however, less than 10 million went to the English banks, against 53½ million to Austria, 162 million to Italy, 195 million to Russia, over 48 million to the Balkan states and so on. Of course the *wealth* of these states did not increase that much more than England's. It was above all the transition to gold currencies which caused such a quantity of gold to go to Eastern and Southern Europe. This movement, however, chiefly took place by means of loans.

In whatever way the gold owners may use the additional gold, it always serves like the other gold, to buy commodities, means of consumption, means of production, and means of destruction. The demand for commodities is increased thereby, and prices rise.

If this increased demand generated no rise at all, or no corresponding rise, of [commodity] prices, then the greater productivity of gold mines would yield, for the capitals invested in them, profits higher than the average rate of profit prevailing in the capitalist world, generating a migration [to gold mining] similar to that which occurred, in the same case, under simple commodity production. Only that formerly the higher productivity in gold production directly attracted increased labour power to that industry. That ceases now, because the increased yield does not go to the workers. Still, this yield causes an increased stream of capital to flow into gold mining, which under these conditions now yields a greater profit than the average. The increased capital then also attracts increased labour power, without which, after all, it cannot be applied.

New capital and new labour power will thus now go into gold mining if, despite the increased demand, commodity prices do not rise enough to equalise the difference in the rates of profit. The additional capitals and labour power produce new, additional quantities of gold, which in turn again create a greater demand for commodities and drive their prices further up.

The stream of new capital to gold mining will last until the rise in commodity prices has reached such a point that the extra profits of gold-producing cease and the rate of profit in

[168] Roberts 1912.

gold mining is the same as in the other branches of production. Indeed, it can go so far as to reduce the average rate of profit in gold-mining below the general rate of profit, for the same reason that the purchasing power of gold is beneath its exchange value [See section one]. The lottery character of gold mining, which is inherent to it also under capitalist exploitation, attracts numerous capitalists, who invest in mines with very low profitability. Varga in his article (1911) has given some dramatic examples of this. Just compare the dividends in the following two South African gold mines:

	1901	1902	1903	1904	1905	1906	1907	1908	1909	1910
Ferreira	–	100	287.5	250	262.5	300	300	300	600	300
General Mining	–	10	10	–	20	–	–	–	5	15

The proceeds thus vary between 0 and 600 per cent.

As you see, it is quite a lottery.

In the special report on mining issued by the American Census Bureau [based on data taken from the census of] 1900,[169] Dr Isaac Hourwich discussed *Gold and Silver* (pp. 500–80).

Dr Hourwich gives the following figures for 1,079 companies engaged in gold and silver mining in the United States:

	Paying dividends	Not paying dividends
		In full operation
No. of companies	136	614
Outlays for labour power in dollars	13,200,000	19,400,000
Other operating costs in dollars	7,500,000	10,000,000
Value of the product in dollars	35,300,000	31,600,000

Thus only a small number of gold mining companies paid dividends in 1902. They were admittedly the largest. They produced more than one-half of the total product. Those not paying, however, employed much more labour than those paying. A similar relation cannot be found in any other industry.

Just as in lotteries, it is also here especially the small people who are robbed of their money by the organisers of the lottery, the promoters. Shares are in advance adjusted for this purpose, and are issued at the smallest possible sums. According to the above-mentioned

[169]Department of Commerce and Labor, Bureau of the Census, Special Reports, *Mines and Quarries 1902*, Washington, 1905.

report, the dividend-paying companies have no less than 94,700,000 shares at an average of two dollars per share (8 marks). There is democratisation of capital for you! Every workingman can become a capitalist, an owner of gold mines.

The sums paid out as dividends on these shares amounted to 10.5 million dollars, or a little more than 5 per cent on the amount invested.

There is, however, the enormous number of 516,000,000 shares of those companies which paid no dividends! The democratisation of capital was here still further advanced. The average nominal value of a share was 1 dollar and 60 cents. The glittering gleam of gold, so universally attractive, emptied the pockets of its pursuers to the extent of $834 million, leaving them merely with pieces of paper which paid no dividends. These operations were, however, veritable gold mines for the promoters and agents.

On the whole, in 1902 four billion marks were invested in American gold and silver mines and 50 million marks were distributed as dividends, about one per cent!

Altogether, the capital in mining in the United States consists of shares representing 2,900 million dollars, on which dividends to the amount of 72.5 million dollars were paid in 1902. Thus we find:

	Gold and silver mines	Other mines
Share capital in dollars	1,017 million	1,886 million
Amount of dividends in dollars	10.5 million	62 million
Average per cent by dividend	1 per cent	3.33 per cent

This shows that the profit rate in the production of gold and silver is far below the average.

So far we have been considering the effects of a change in the methods of producing gold under capitalist production that are analogous to those we had observed under simple commodity production. But the effects of an increased production of gold upon industrial production under capitalist relations are quite different.

One of the hallmarks of simple commodity production is stability. It takes place year in, year out in the same way, undisturbed by stagnations of the market resulting from general overproduction, but also [from] too rapid expansion. Each handicraft requires its special workforce, differentiated by long training, which cannot be employed in other handicrafts. Every now and then can be found, already under this mode of production, a numerous proletariat of unemployed, but it is a lumpenproletariat which, under the given technical conditions, cannot be involved in the production process. This is prevented not only by the

requirements of educated craftsmanship but also owing to the lack of additional means of production for additional labour power.

The capitalist mode of production is different. In *Capital*, Marx shows in detail the methods by which on the one hand an industrial reserve army is formed, and, on the other, capital is bestowed with an enormous elasticity [*Schnellkraft*]. Through both of them together, temporarily the *most rapid* extension of production is rendered possible, whose *constant* expansion through the accumulation process becomes a vital necessity for the entire capitalist method of production.

I must presuppose here that Marx's views on this issue are well-known.

Under these [capitalist] conditions, the expansion of gold production has a completely different effect than under simple commodity production. A rise in gold production under the latter brings about an increase of prices in the commodity market, without stimulating commodity production, often indeed with the effect of siphoning off its forces and thereby constricting it.

Under the capitalist mode of production, in contrast, every increase in the demand for commodities acts as a spur to extend production, a spur which the process of production immediately and readily obeys.

The increased amount of gold, which appears upon the commodity market and generates an increased demand for commodities, raises their prices and therewith the profits to be had from their production. So, now not only the production of gold but all the other branches of industry, incited by it, require new capitals and with them also additional labour forces. The capitalist mode of production has enough of them both, and the expansion of gold production by no means exhausts the industrial reserve army.

One might certainly imagine that in the capitalist mode of production the increased demand for gold would soon be compensated by an increased supply of commodities and that in this way the previous level of prices would be restored. But that would imply nothing else than a restoration of the extraordinary profit rate in gold production. As a result, increased capital would again flow to it, gold production would expand again, the demand for commodities would be again increased, and prices would again rise, which would give a new impetus to the production of commodities and so forth. If the increase in gold production is not temporary but long-lasting, it must have a very deep influence on the process of production. Let us assume that the increased quantities of gold at first only increased the demand for machinery (for the new mines), for palaces for the gold upstarts, for beer and meat and textile products for men and women servants, and for the wage workers in the gold mines.

This means again an increased demand for iron and coal and wool and cotton, for brick and stone, for spinning and weaving machinery, for malt and hops and corn and butchers' meat, etc. The profit and the sums spent in wages in all of these industries must consequently rise. Besides, they generate new demand for means of consumption and production of all kinds. If this process lasts enough time (and according to our presupposition it is stimulated again and again by the steady appearance of new gold on the market), we have a thoroughgoing era of prosperity steadily marked by a general rise in prices.

This rise in prices now appears, when it becomes general, to operate against the increase of the profit rate in industry, because it increases the price of its raw materials and wages, and thereby it appears to restore the superior profit rate in gold production which existed at the beginning of the improvement in the conditions of production, before the rise in prices. Insofar as profit depends upon prices, it is determined by the *difference* between buying and selling price. If, accordingly, the price of a manufactured commodity rises, but simultaneously with it grow also the prices of raw materials, of machinery and of labour power, profits do not increase, indeed they may even diminish if the price of the latter factors increases more rapidly than that of the manufactured product.

However, the rate of profit does not depend only on the differences in prices. It is annually calculated according to the mass of profit pocketed by a given capital in the course of the year. This total mass does not depend only on the amount of the profit which the capitalist obtains from each individual transaction but also on the number of transactions which he made in the course of the year. If the capitalist does not have to store his commodities for a long period, but sells them rapidly and is immediately paid for them, he turns over his capital quickly and thereby increases his annual rate of profit, even if the profit realised on each turnover remains the same. Indeed, it may even increase his annual rate of profit even if the profit on each separate transaction decreases.

Let us assume that the capitalist earns 10 per cent on each turnover of his capital, and that he turns over his capital twice a year; that means an annual rate of profit of 20 per cent. Let us further assume that the increase in the price of raw materials and the rise in wages reduced his profit on each turn-over of his capital to 5 per cent, but the vigorous course of business enabled him to turn over his capital six times a year, so that his annual rate of profit is 30 per cent.

An increased demand for commodities brings about this vigorous course of business, this acceleration of the turnover of capital, and thus increases profits despite the general increase in prices.

In the production of gold it is impossible to increase the rate of profit through a more rapid turnover of capital, since the turnover depends on the conditions of the market and not, for instance, on technique. The transformation of money into commodities and of commodities into money in the market does not exist for gold, insofar as it functions as money. The rate of profit in gold mining depends in this sense exclusively on its conditions of production and not on the speed of commodity circulation. Gold is money as soon as it is produced, that is to say, as soon as it is brought to the market. It does not have to wait for a buyer to turn it into money.

The rise of the profit rate through the acceleration of commodity circulation therefore pertains exclusively to capital invested in the production of commodities. In that way, the flow of capital to gold mining is kept within certain limits. As soon as the production of new masses of gold begins, a brisk demand for commodities develops and stimulates the production as well as the turnover of those commodities.

Precisely this stimulus, this acceleration in the production of commodities, goes hand in hand with a rise in prices, as each period of prosperity shows. Bringing about such an epoch of prosperity and with it an increase in commodity prices, *that* is the method by which, under capitalist conditions, the law of value asserts itself in gold mining, given a reduction of the labour time socially necessary for the production of a given amount of gold. Only when this method is not sufficient, does the movement of capital into gold production for the equalisation of the profit rates additionally join it.

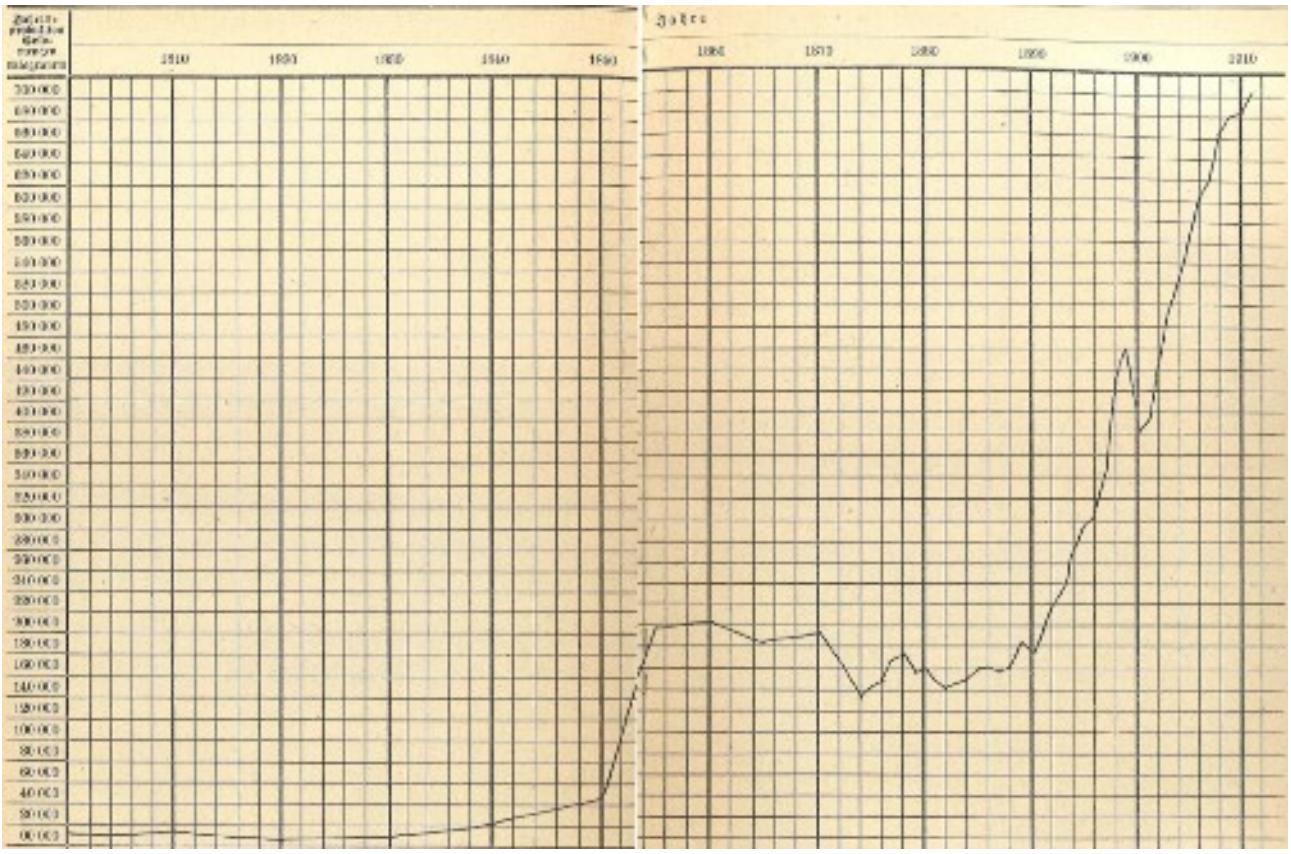
The contention that changes in gold production have contributed to the present rise in prices therefore remains unshaken, despite Varga's arguments to the contrary. He points out that the world production of commodities has experienced an enormous increase in the last decade (for example, from 1900 to 1909 the iron production grew by 50 per cent, that of coal by 35 per cent, copper by 61 per cent, wheat by 31 per cent, cotton by 45 per cent, etc.), and he opposes to this the fact that the amount of gold used for monetary purposes during that period grew by only 32 per cent (Varga 1911). That is certainly a convincing argument against the quantity theory, which seeks to explain the rise in prices by a mere comparison between the level of commodity prices and that of the heaps of gold, but it proves nothing against my view that, under capitalist commodity production, the prosperity arising from increasing demand constitutes the mechanism which adjusts prices and profit rates to improvements in the conditions of production of gold and through which the law of value asserts itself in the case of gold.

Varga would explain that the period of prosperity which we have gone through for nearly

twenty years has nothing to do with the changes in the conditions of production of gold and was due to entirely different factors.

If he wants to show that the law of value does not apply to the money commodity, he must prove that an increase in the demand arising from increased gold production has no influence on commodity prices, commodity exchange, or commodity production. He would find this hard to prove.

I believe that I have shown, theoretically, how increased gold production must operate in this connection. The actual statistics support my theoretical conclusions (see the chart).



For the drawing of the line from 1800 to 1850, we do not have figures for individual years, but only for decades. So they do not show the annual variations, but only the general tendency of the decade.

Besides gold extraction, silver extraction comes into consideration for an analysis of the influence of the production of the precious metals on economic life. Here we must abstract from the latter in order to avoid complicating the exposition. We will only say the following about this:

Till the middle of the 1870s there was barely a change in the relative value of gold and silver during the whole nineteenth century, not even in the 1850s, at the time of the rising

production of gold. Gold steadily remained fifteen times as valuable as silver. There was a speedy change in the 1870s following upon a rapid change in the method of producing silver. In 1870 the ratio was still 15.57 to 1, in 1879 about 18.39 to 1, in 1889 about 22.10, in 1898 35.03 to 1, in 1909 39.74 to 1, in 1910 38.22 to 1, finally in 1911 38.33 to 1.

Under those circumstances, it was impossible to retain both silver and gold as measures of value. All the states that were involved in world commerce and that up to then had a silver or a double currency found themselves practically, if not always formally, obliged during the last quarter of the nineteenth century to adopt the gold currency.

Silver money was not thereby completely eliminated; it was merely reduced to the role of token coins [*Scheidemünze*]. Silver coins no longer function as the representative of their value in silver but of a certain gold value established by law. Like paper-money, silver can only fulfil this function as long as its output is confined within certain limits. But these are very broad. The so-called demonetisation of silver, the discontinuance of its role as full-valued [*vollgültiges*] money proper, has not ended the coining of silver money. It has merely brought about that silver money does not suffer the effects of the fall in the value of its metal and henceforth is accepted as a certain amount of gold. The purchasing power of a single silver coin, the demand that it is able to develop, has thus by no means diminished in proportion to the reduction in the value of silver, but only in proportion to the reduction in the value of gold.

But the demand for token coins grows rapidly with the development of capitalism, partly through the development of the wage system, by which the number of wages earners increase and at the same time money payments increasingly take the place of payments in kind. Both cause the sum of money wages to grow enormously and these are for the most part paid in token coins.

Thus, for example, in the United States from 1880 to 1910 the number of wage workers in industry alone increased from 2,700,000 to 6,600,000 and the annual amount of their wages from 950 million to 3,400 million dollars.

This increase in the sum of wages paid caused an increase instead of a decrease in the amount of silver money, despite its demonetisation.

We can know the amounts of silver money which have been newly coined since its demonetisation from a review by the Director of the United States Mint in his recently published report. According to it, in the last thirty years (1880 to 1910) gold coins for an amount of 8.77 billion dollars and silver coins with a mint value of 5.4 billion dollars have been minted in the entire capitalist world. This includes, of course, a great deal of reminting

of old coins or minting of remelted old material. The amount of the available stock of money metal must be estimated at much less. The report estimates the amount of money lying in the banks of the most important countries in the world in 1910 at about 5 billion dollars, and the amount of gold in circulation at about 2 billion dollars. The amount of silver money it estimates at about 2.6 billion dollars.

Through the demonetisation of silver, the mass of money which it represents, at any rate its purchasing power, has not lost its economic effect. But one should not conclude from it that this phenomenon has counteracted or inhibited the economic influence of increased gold production.

If we examine the chart (see previous) we shall find a rapid rise soon after 1850, as a result of the discovery of gold fields in California (1848) and Australia (1851). These discoveries began to operate on the English labour movement immediately after the disillusionment of 1848. They quickly attracted many of its most energetic and dissatisfied elements, who went off to the gold fields, and by this Chartism was significantly weakened, just as the Reformation lost its strongest props in Germany owing to the gold and silver discoveries in Spanish America. On both occasions gold strengthened the counterrevolution. At the same time, changes in gold production exerted their economic influence on the production of commodities.

Marx and Engels were the first to point out the significance of the California gold discoveries. Already in 1850 they declared the discovery of these mines to be 'more important even than the February Revolution' (MECW, Vol. 10, p. 265). It brought to England that 'intoxicating augmentation of wealth and power' of which Gladstone spoke in his speech on the budget in 1863; and which Marx quoted a year later in the Inaugural Address of the International.

This was the brilliant period of the [Second] French Empire [1852–70]. A rain of gold seemed to pour on 'good society'. Also in France we find a brilliant course of business and a fever of promotion and speculation. Finally, that period laid the foundations for the rise of large-scale industry of Germany, which from that time on developed rapidly.

From 1860 the growth in gold production came to a stop, but it continued to have an effect for a while. From 1870 to 1874, by contrast, we find a marked decline in gold production, followed by a considerable fall in prices, and then, with the stagnation in gold output until the beginning of the 1890s, a period of lower prices and continued stagnation, which caused many of us (I admit I was one of them), to think that the capitalist system had already fallen into a condition of chronic overproduction.

But suddenly began a new upturn in gold production, such as the world had never seen before. In the year 1886 the first mine in the South African Rand was opened. In 1890 the

cyanide process was introduced, in 1897 the gold fields of the Yukon in Alaska were discovered.

As this advance in the production of gold made itself felt, stagnation disappeared, prices began to rise, and capitalism entered with full force upon a brilliant phase of its development. The mutual connection of all these phenomena becomes here evident.

Sauerbeck has calculated the prices of a series of staple articles on the London market since 1818. If we fix the price between 1891 and 1900 at 100, we get the following series:

1818	214	1842	137	1866	154	1890	108
1819	183	1843	125	1867	151	1891	108
1820	169	1844	127	1868	149	1892	103
1821	160	1845	131	1869	148	1893	103
1822	152	1846	134	1870	145	1894	95
1823	155	1847	143	1871	151	1895	94
1824	160	1848	118	1872	164	1896	92
1825	177	1849	112	1873	167	1897	93
1826	151	1850	116	1874	154	1898	97
1827	146	1851	113	1875	145	1899	102
1828	146	1852	118	1876	143	1900	113
1829	140	1853	143	1877	142	1901	103
1830	137	1854	154	1878	131	1902	105
1831	139	1855	152	1879	125	1903	105
1832	134	1856	152	1880	132	1904	106
1833	137	1857	158	1881	127	1905	109
1834	136	1858	137	1882	126	1906	116
1835	139	1859	142	1883	124	1907	120
1836	154	1860	149	1884	114	1908	110
1837	142	1861	168	1885	108	1909	112
1838	149	1862	152	1886	104	1910	117
1839	155	1863	155	1887	103		
1840	155	1864	158	1888	106		
1841	151	1865	152	1889	109		

We see here how, up to 1849, with an unchanged gold production, prices sank universally, with interruptions in times of prosperity. From 1849 prices rose, at first unremarkably, and then rapidly from 1853 to 1861. Then they remained about the same until 1873, falling in

times of crisis, rising during the period of economic upswing from 1871 to 1873. Again we have a fall in prices coincident with a stagnant and occasionally falling gold production until 1896. Since then a rise in prices has taken place, which today occupies us all.

Of course, one must avoid throwing the alternation of prosperity and depression connected to fluctuations in gold production together with the alternation of these phenomena arising from the industrial cycle of approximately ten years. This latter circuit is the necessary form of the expansion of the capitalist process of production; the individual phases of this circuit [*Kreislauf*] must repeat themselves at regular periods of time. The first alternation, by contrast, depends on a series of accidents and does not constitute a circuit, its different phases are not bound up in a determined recurrence.

Both movements are in their origin independent of each other, but they cross, intermingle and influence each other in the most diverse ways. The course of gold production is of the greatest significance for shaping the industrial crisis cycle. If the expansion of gold production ceases or weakens, the upturn periods become shorter and increasingly feebler. By contrast, the periods of crisis grow longer. The latter acquires a tendency to take on a chronic character. This happened in the two decades after 1873. It is quite otherwise in periods of rising gold production. The prosperity that it produces does not abolish the crises, but it lengthens the periods of the upswing, makes them more energetic, while it shortens the periods of crisis and depression and makes their termination easier. This is the picture of the industrial cycle of the last two decades.

3. The circulation of money

We must now consider the question – how is it possible that changes in the conditions of production of gold could produce such tremendous changes in the entire economic life, since the production of gold, as compared with the entire world production is only an insignificant fraction? The annual world production of gold is today about two billion marks. Varga contrasts it to the entire value of world production, which he calculates at 124 billion marks. Thus gold production represents only 1½ per cent of the total production, an entirely insignificant fraction.

Gold production would seem to mean very little. But does the way in which the law of value asserts itself with a commodity depend on the magnitude of the share of the total product which it represents? Why should precisely gold be an exception? Is it because it is a commodity of a special kind? But precisely this special nature brings about, that the changes

in gold production have a much greater influence on economic life than the proportion between its amount and the amount of total production would lead one to expect.

We have already examined one of the distinctive features of the money commodity. It consists in the fact that it is a commodity which has a use value for everyone under all conditions, a fact which Varga conveys by saying that the central banks always 'buy' any amount of gold.

But the money commodity does not differ from all others only in this respect. There is yet another, very substantial difference. If we abstract from intermediary trade, which merely obscures but does not alter our present problem, commodities merely experience one single movement in the commodity market: they are exchanged by their owners and then cease to be commodities, disappear from the market in order to be consumed sooner or later. The producer sells them to the consumers; they play no further role in the commodity world.

It is otherwise with money. Once on the market, it does not leave it. Its movement inside the capitalist mode of production is therefore a double one. Some of the money is spent as *revenue*, as the income of capitalists and wage workers, for the satisfaction of their personal needs. The money spent in this way does not return to its original source. Another portion of money is spent as *capital*, either for the application in the capitalists' own enterprises, or as loans to other entrepreneurs. This money has the distinctive quality of returning to its original source, there to appear increased by a surplus value. Diverse as these two different forms of the movement of money are, they are both constantly at work on the market. There the money commodity lives, disregarding wear and tear, an eternal life; while the commodities, once they are bought by their consumers, either as articles of consumption or as means of production, disappear from the market forever.

It is thus not acceptable to confront the annual production of gold with the annual production of commodities and to assess the significance of the former by comparing it with the magnitude of the latter.

This holds true in two directions. First, the annual production of gold develops a much larger demand for commodities than its size would imply, and second, the annual production of commodities disappears from the market in the course of the year, to make room for new production, while the mass of money, which during the year enabled the produced amount of communities to circulate, remains in the market, increased by the annual production in gold.

Let us the case of simple reproduction, that is, when the same amount of commodities are produced, year in, year out. Here any production of new gold would be entirely superfluous, if we abstract from the insignificant amount required to make up for the wear and tear of

coins, as well as from the industrial employment of gold to create jewellery, utensils, watches, and the like, with which we are not at present concerned. No matter how big the annual production of commodities may be under simple reproduction, or how small the annual gold production for the making of new gold money, the latter must bring about, given a constant supply, an increased demand for commodities and thus a rise in commodity prices, which would soon put an end again to the production of gold [for the making of new gold money, over and beyond that required to make up for the wear and tear of coins].[170]

Abstracting from the industrial use of gold, and assuming new gold production with constant conditions of production, gold can only preserve the same value, on the long run, with expanded reproduction, whose scale grows from year to year.

If one wants to compare the annual production of gold with the annual production of commodities, it should not be done by confronting the annual gold production with the total mass of commodities produced in a given year, but by comparing that amount of gold (insofar as it does not replace worn out or industrially consumed gold) with the increase which commodity production has experienced in the year under consideration over the previous year.

As soon as this is done, the annual sum of produced gold ceases to appear as a trifling magnitude within world production.

It is impossible, given the present state of statistics, to calculate the amount by which the world production of commodities rises annually. But merely as an illustration we can take the figures of world trade, which have been more accurately gathered annually and about which we may assume that they grow in the same measure as the increase in world production. The total trade of the world in 1910 was about 146 billions of marks. This number doubles the actual volume of trade, as what appears as exports from one country appears also as imports into another. It must be halved. Accordingly, in the year 1910 the value of world trade was in the neighbourhood of 73 billion marks. In the year 1902 the total world trade amounted to about 48 billion marks. From 1902 to 1910 there was thus an increase of 25 billion, about three billion annually on the average. Varga calculates world production today at 124 billion marks, thus a little less than twice the present world trade (73 billion). If we assume that world production amounts to twice the amount of world trade, we are estimating it very highly. We cannot put the annual increase in world production today at more than 6 billion marks a year. As against these figures, the annual gold production of 2 billion marks is no longer a vanishing quantity: it amounts to a third [of the annual increase

[170]See Marx 1978, pp. 400ff.

in world production].

We are here, as we said, not making exact calculations of real proportions but just illustrating them, and for this purpose the above-mentioned figures are enough.

That the significance of the annual production of gold is quite different if it is compared with the annual *increase* in production and not with the mass of total annual production is perfectly clear and needs no proof. But it cannot be denied from the outset that the significance of gold production may be overestimated by this comparison, as the figures furnished are quite uncertain.

However, we may not be satisfied with comparing the annual increase of world trade or world production with the annual gold production. We know already that things are not as simple as they appear in the quantity theory [of money], which places on the one hand the gold heap and on the other the mass of the other commodities, and says that the price is a result of a comparison between the two.

Market demand depends not just on the amount of gold appearing on it, but also on the speed with which it changes hands. The same amount of gold will produce quite different effects where it mediates exchanges ten times a year, than where it does it only twice. A hundred marks will in the first case create a demand of a thousand marks a year, in the second case of only two hundred.

The increased demand for goods resulting from an increase in gold production is a very significant factor in determining the total demand and the total production process, but it is by no means the only factor that works to that end.

Have any peculiar circumstances appeared in the course of the last twenty years that have tended to annul or weaken the effects of increased gold production?

We know already that the intensity of these effects depends on the speed of the process of commodity circulation, a speed which, again, is determined partly by technical and partly by economic causes. Means of transportation play a great role in this respect. How far they have developed in recent times requires no demonstration.

An additional factor which increases the speed of commodity circulation is the use of money as means of payment. Up to this point, we have proceeded from the assumption that commodities are always exchanged for money, that is, that they are sold for cash. But at a certain stage in the circulation of commodities, arrangements appear which allow me to buy someone else's commodities before I have sold my own commodities and obtained money for that purpose. I buy someone else's commodities for a mere payment promise, whose fulfilment will fall due at some future time, perhaps three or six months. It is clear that the

turnover of commodities can be accelerated very much in this way.

It is true that when I make my final payment, I again use money. But when numerous payments are concentrated at specific points in money traffic it soon happens that many outstanding bills cancel each other out, and that they can therefore be settled without any real money having been spent. However, one cannot venture at will too far away from metallic circulation, which always remains the foundation of payments. This is so because not the all payment obligations can be compensated with others. Whoever only has to pay and has no payment to demand, or whoever has more to pay than he has to demand as payment, must pay cash. Besides, this whole mechanism of payment promises and settlements is also very sensitive to any disturbance and threatens, in such cases, to bring about a complete standstill in the circulation of commodities, which happens all the more easily, the more insufficient are the existing money stocks to settle the arrears. Adequate reserves of money must always be available to overcome stoppages.

Purchases by means of payment promises and their mutual settlement cannot therefore make cash money superfluous and eliminate it. But if we have previously seen that the expansion of the production and circulation of commodities, all other things being equal, calls forth a corresponding increase in the amount of money in circulation, we now learn to know the opposite phenomenon. The more massive and concentrated the payment liabilities, all the more mutual demands will be settled, and all the less real gold is required to keep the circulation of commodities afoot, the smaller can be the available amount of money in proportion to the volume of commodity circulation. The mass of gold declines not absolutely but relatively; the volume of commodity circulation can grow more rapidly and does grow more rapidly than the money supply. The economic effects of the existing mass of gold will be increased, and therewith also the impetus will be increased which each additional amount of money imparts to the production and circulation of commodities.

It is well known that a great expansion of the mechanism of credit has taken place in the last decades.

Just as important are the conditions of the market. They, too, have been particularly favourable during the last twenty years. With the growth of the mass of gold and spurred on by it, as we have seen, an era of prosperity unfolded in which the circulation of commodities has been tremendously accelerated, which heightened the effect that the increased masses of gold had on demand. The rapidity of commodity circulation does not counteract the consequences of the increased gold production; on the contrary, it works in the same direction and intensifies its tendencies.

And the same has occurred with the other circumstances affecting the degree of influence of gold production [on the production and circulation of commodities].

Not the whole product of the gold mines is converted into money. A portion enters industry as raw material and becomes not money, but commodity. This portion develops no demand for commodities, it is itself a commodity which seeks a purchaser in the market and wants to be exchanged for money. The greater the portion of the annual gold production used industrially, the smaller the portion which will be turned into money, and proportionately smaller, all other conditions being equal, the effect of gold production on the stimulation of the market and the rise in prices.

But all this does not in the least imply that in the last twenty years a change has occurred which has lessened the share of annual gold production that is converted into money. Quite the contrary.

Before the emergence of commodity production, the working of gold and in general money metals into articles of use was naturally their only use. It was also predominant at the beginning of commodity production. The function of gold as money proceeds from the fact that it is a use value sought after everywhere, which does not change with use. The collection of gold and silver jewellery and utensils is, under simple commodity production, no mere luxury, but also a form of collecting treasure. The capitalist mode of production is the first to transform money into capital which brings profit, so that every piece of gold which one does not use as money is regarded as a cause of loss. As a result, the industrial employment of gold has been significantly limited.

The opening up of new and richer areas for capitalism goes on apace even today, particularly in Asia, with its pre-capitalist modes of production. That means that the process of restricting the industrial use of gold for the benefit of its transformation into the money form goes on even today.

There is, of course, an opposite tendency, namely the increase in the exploitation of the proletariat, the increase in the mass of surplus value, and with it also the increase in the consumption fund, in the revenue of the capitalists, which adds to their demand for luxury articles. But the capitalist does not like to reduce through his luxury precisely the circulation of the money commodity, the life-giving blood of the capitalist body.

Finally, there is still another factor to be considered. Gold as money is capable of indefinite employment and extension. Gold worked industrially is, by contrast, a commodity whose sale depends on needs which for the most part are set by tradition and do not quickly change. A sudden expansion of gold production will therefore increase its use for industrial purposes

less than its use as money. But of course, on the other hand, a diminution in the production of gold will diminish the quantity used for industrial purposes less than that used as money. All these considerations give us reason to believe that the use of gold as money has developed in the last twenty years more than gold production itself.

The statistical proof for this statement is not easy to furnish, since, for that purpose, one must have exact figures for the different kinds of use of gold in the whole world for decades. In the absence thereof, we are compelled to offer estimates. These, however, substantiate our expectations based on theoretical considerations.

Neumann Spallart calculated the gold production for the years 1881 to 1885 at 746,000 kilogrammes, of which the greater portion, 424,000 kilogrammes, was destined for industrial use in the countries of capitalist civilisation. Soetbeer came to a similar conclusion. The already frequently quoted report of the director of the United States Mint investigates the industrial employment of gold for every year since 1890. I have calculated according to his figures the percentage of the amount of annually produced gold which is employed industrially.

Year	Gold Production Value in millions of dollars	Industrial use of gold in millions of dollars	Percentage of industrial use of gold
1890	119	50	42
1891	131	50	38.5
1892	147	50	34
1893	157	51	32.5
1894	181	53	29.2
1895	199	59	29.6
1896	202	60	29.7
1897	236	60	25.4
1898	287	66	22.9
1899	307	73	23.8
1900	255	76	29.7
1901	261	79	30.2
1902	297	76	25.6
1903	328	75	22.9
1904	347	78	22.5
1905	380	81	24.4
1906	403	96	23

1907	413	97	23.4
1908	442	89	20.1
1909	454	101	22.2
1910	455	112	24.6

The industrial use of gold thus grows absolutely, but not as rapidly as gold production. At the beginning of the 1880s it was still the larger half, in 1890 still more than two-fifths, in 1907 only one-fifth. Since that time it has grown a little, to one-fourth. While the production of gold has quadrupled, the industrial use of gold has only doubled. We can see that it has a much more conservative tendency than the production of gold. It increased in 1900 and 1901 just as it did earlier, although at that time the Boer War conspicuously diminished the production of gold. In recent years the tempo of gold production slowed down, but on the other hand its employment in industry showed no change in its tempo, so that its share in gold production since 1908 has increased, even if not as rapidly, to the level of 1900.

No less important for the economic effects of the annual gold production than the proportion of its use as industrial raw material or money is the extent of its use as *treasure* or as circulating *coins*.

Up to a certain point, it rests with the owner of money whether he will spend his money and thereby create a demand for commodities or put it in his pocket and pile it up in his safe as treasure. The more he does the latter, the less will the existing amount of gold stimulate the demand for commodities and raise their prices.

However, it does not depend altogether on the wish of the money owner whether he will spend his money or not. He is the tool of an economic necessity. When the workman receives his wages, he must spend his money or go hungry, however much the bourgeois economist may urge him to save. And also the entrepreneur has no freedom of choice as to whether the money that he gives away for commodities had to be spent or accumulated as treasure. He must spend a part of his money, like his workman, in the necessities of life. He must dispense with another portion for tools and raw materials and wages, and he must keep on producing and bringing new commodities into the market if he is to keep on living.

The necessity of rapidly spending the money received is, on the whole, much less pressing with simple that with capitalist commodity production, because wherever the former is dominant it is not the general form of the whole production, but appears as a concomitant phenomenon to the predominantly natural economy. If the peasant for the most part produces the goods that he consumes, the artisan also often practices some farming. And the

tributes to the great exploiters are mostly paid in natural products. The compulsion to spend money, gold or silver, which has to be got in any way for the purpose of consumption or for the continuation of production, is not nearly as urgent as in the capitalist mode of production, and the possibilities for the profitable investment of money are minimal. Still, the control of the money metal, even at that stage, gives great power. Hence, under such primitive conditions, the striving to accumulate treasures of precious metal, either in the form of utensils and ornaments which can be converted into coin or in the form of actual coins.

There are two ways of getting possession of such a treasure, the one peaceful, by the exchange of commodities against money which one does not spend, the other, the forcible one of robbery. In simple commodity production the first method is as a rule slow, since the surplus which a man can get by his labour is small. Not only the worker but the exploiter receives under such circumstances only small sums which can be saved. Plunder is quite different. Whoever plunders by armed force may get the accumulated treasures of numerous exploiters and accumulate great riches.

Under capitalist conditions, the reverse is true. The productivity of labour has increased so much that the surplus which a single labourer produces over and above the cost of his maintenance is quite significant. At the same time, the opportunities for individual exploiters to exploit increasingly large crowds of workers all at the same time grow more and more. By peacefully buying labour power it is possible today have a huge annual income.

In proportion as capitalism grows, the power of the state also grows, the security of property grows, and the possibility of getting treasure through robbery is diminished. Therewith changes the moral estimation of the two methods.

Under simple commodity production, the peaceful accumulation of treasure was despised as miserliness, and the booty-making war hero was praised. Today, he is considered a criminal, if he acts on his own, while the capitalist who makes billions from the overwork and the undernourishment of many thousands of workers is glorified.

Marx once justly remarked that theft is not a mode of production. But it has long constituted a strong economic factor, particularly where it has been carried on, not by individual highway robbers, but by the warlords of whole nations. By war and plunder immense masses of money can be transferred from one country to another. In the sixteenth and seventeenth centuries enormous amounts of precious metals overflowed Europe and caused a revolution in prices, but the discovery of very rich finds in America, of which we have already spoken, was only one of the causes thereof. The other, at times even more important than the real

cause, was the plundering of great treasures of gold and silver which had been piled up by the labour of centuries in certain places of the newly-discovered districts.

If gold and silver production in Spanish America then depopulated Spain and reduced its industrial labour power, as we have already shown, that happened only to a small extent because the Spaniards were miners in America. The workers in the mines of the Spanish colonies did not come from the metropolis, but were Native Americans. But the occupation and mastering of the colonies, the plundering and the division of the booty cost so many men, that the rich stream of precious metal obtained in this fashion resulted in a diminution of industry and drowned, not fertilised it.

We find numerous similar examples under simple commodity production. The most conspicuous example is furnished by ancient Rome, into which flowed the gold and silver treasures of the whole world. Also these treasures created no extensive new industry in Italy; they flowed off to the districts with more highly developed industries, which in the end were enriched by it. Roman spoliation deprived Spain, Gaul and Raetia of their gold, not in order to hold it, but to buy Asiatic luxuries with it, insofar as it was not needed for the payment of German mercenaries.

After Rome's military power was gone and its ability for fresh spoliation came to an end, it quickly grew poor in precious metals.

The results are entirely different when such treasures, which were accumulated under pre-capitalist modes of production, flow through plunder to states with capitalist industry. Then they become means of developing it more quickly than the mere development of gold production would permit. The precious metals of Spain, obtained in America, flowed by means of trade into France, Holland and England, insofar as they did not fall into their hands through piracy. Next to it, the spoliation of the East Indies was the means of bringing a vast amount of treasure into England. The Indian luxury industries had, ever since the time of the Roman Empire, exchanged uninterruptedly their commodities for gold and silver, and the Indian lords had, for fifteen hundred years, steadily piled up the money received into mighty treasuries, which were then all at once brought to Europe.

When Clive, by the battle of Plassey, 1757, founded British power in the East Indies, the treasury of Bengal was, as Macaulay says, 'thrown open to him':

> There were piled up, after the usage of Indian princes, immense masses of coin, among which might not seldom be detected the florins and byzants with which, before any European ship had turned the Cape of Good Hope, the Venetians purchased the

> stuffs and spices of the East. Clive walked between heaps of gold and silver, crowned with rubies and diamonds, and was at liberty to help himself.[171]

The Reformation and the French Revolution also transformed the substantial gold and silver treasures obtained through the plunder of churches and monasteries into money.

These methods of spoliation which created masses of circulating money out of the treasures, and which thereby suddenly expanded the demand for commodities and the capitalist production process, gradually ceased in the course of the nineteenth century. This is not because respect for the property of a nation defeated in war has increased, but because pretty much all the great treasures to be found outside the capitalist mode of production have been plundered. What plunder still survives today, like the looting of Beijing after the suppression of the Boxer Uprising, is relatively unimportant, although it has brought a nice pocket money to the robbers themselves.

Giant money transfers from one country to another happen even today – the largest of which was the war indemnity which France had to pay to Germany in 1871. The five billions francs gave a colossal impetus to German industry, but the mass of money which circulated in the world market was not substantially increased thereby. Even so, French borrowing must have served to put existing metal hoards into circulation to a very great extent.

Be that as it may, the old method of turning hoards of precious metal into circulating money through plunder exerts today only small and constantly diminishing effects.

But the more this method declines, the more capitalism develops peaceful methods for drawing the money treasures out of their hiding places and throwing them into the stream of circulation.

If simple commodity production develops a tendency towards boundless hoarding of gold and silver, the capitalist method of production replaces the hunger for gold by a hunger for profit. The accumulation of 'idle' money treasures is now regarded as a sin against the Holy Ghost of capitalism. The first duty of the possessor of money now appears to be the expenditure of money, but only in a productive way, by which the capitalist understands, in a profit-making way.

But also the capitalist must not throw all the money at his disposal into the circulation process of commodities. The production process itself impels him to hoard a part of it. Capitalism creates in place of the old eagerness to hoard gold and silver new conditions and requirements of hoarding.

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[171] Macaulay 1910, p. 63.

Let us take, for example, a factory-owner. His machines cost 100,000 marks. Experience makes him expect that they must be replaced by new ones after ten years' use. In order to do this the capitalist must put away 10,000 marks annually for ten years out of his income.

Or let us take an agricultural large-scale enterprise. In autumn the farmer sells his crop. But he cannot spend the money received all at once. With it he has to live until the next harvest, pay wages, and so on. He must therefore store up his money in the autumn in order to spend it in the course of the year.

Then again, the formation of hoards for consumption purposes, admittedly of a less extensive nature, it also necessary. The workman who wants to buy a winter coat for 50 marks in the fall must set aside 2 marks a week for 25 weeks out of his weekly wages. If he gets his pay quarterly he must therefore make a 'hoard'. And owing to the insecurity of his position it is in the highest degree advisable for him to save a hundred marks or so, so that in case of sickness or unemployment he is not confronted by blank destitution, so long as he has no union or sick benefit fund to protect him.

The more the capitalist method of production develops and replaces natural economy, the greater is the number of enterprises and households needing a greater or less amount of hoarding. Thereby again great masses of gold would be withdrawn from circulation and prevented from developing a demand for commodities on the market.

But this new tendency is soon overcome and forced back by a stronger one.

Let us take again the example of the factory-owner, let us say the owner of a spinning factory, who according to his experience must buy within ten years 100,000 marks worth of machinery and for this purpose must set aside 10,000 marks every year. Let us suppose that the factory owner has already been saving for five years when a neighbour, a brewer, needs money to expand his brewery. He borrows the 50,000 marks from the spinner, who had this sum lying unused in his safe and lends it against the payment of interest to the brewer, if he agrees to repay the loan after five years. All parties benefit from this plan. The brewer increases his operation and makes 20 per cent annually on the 50,000 marks of borrowed money, of which he pays 5 per cent to the spinner. The latter makes 5 per cent annually and has at the end of the ten years the whole of his capital to renew his machinery. His accumulated hoard has, for a portion of the time at least, been thrown into circulation and has increased the demand for commodities.

Such use of hoards is naturally only accidental. Not every industrial capitalist has the time and inclination for such incidental business. This method, moreover, cannot be used for small amounts.

But in the course of time there arise special enterprises, banks, for the purpose of collecting hoards of this sort and lending them to entrepreneurs to start or expand their businesses. They admittedly also become means of increasing state debts, the consideration of which we will abstract from here. The collection of multiple greater and lesser hoards by the banks and their capitalist employment is still further promoted once the stock company [*Aktienwesen*: stock exchange] develops alongside credit.

Even the smallest sums of money are today invested in the capitalist countries with the expectation of earning interest, either as savings or as shares – we called attention to the gold mine shares at two dollars each. These expectations are often disappointed in the share market, but the [interest-bearing] effect of the transformation of hoards into circulating money is more secure.

This development has made rapid strides in the last twenty years and therewith powerfully supported the effect of the increased gold production on the market. In a similar direction operate the improvements in transportation which permit a reduction in the amount of stocks which the individual companies have to pile up and consequently the sums of money which they have to hoard for that purpose.

Individual banks admittedly cannot exist entirely without hoards. If the amounts of their payments [out] never exceeded their simultaneous [incoming] receipts, the banking business, as far as it fulfils the function we are here discussing, could be carried on without any capital. As a rule there is an excess of receipts over payments made, if not by an individual bank, then by the banking business as a whole, because the accumulation of capital and the collection of newer, additional sums of money goes on uninterruptedly.

But there come times of stagnation, when the movement of money takes an opposite course. A crisis breaks out, which is bound up with high unemployment, and the workers are compelled to draw on their savings instead of increasing them. At the same time, the industrialists cannot dispose of their commodity stocks. To live and to be able to produce further, they must withdraw their deposits from the banks or sell their shares. It is bad for the bank which under such conditions had put its capital into shares, instead of having accumulated it as cash, which admittedly draws no interest.

But even in times of good business, there come deadlines at which payments cluster and an unusual amount of money is needed. Also for such deadlines the bank must have a large supply of cash in readiness.

But however much money the banks must hoard to meet the sudden requirements and unexpected demands for money, their hoards are always much smaller than the sum of

private savings which they attract and turn into circulating money.

One must not imagine that the total amount of money which a bank collects functions as hoard. The great central banks accumulate enormous amounts of gold. For example, according to the report of the American director of the Mint, the amount of gold in millions of dollars was:

Year	Bank of England	Bank of France	Bank of Germany	Bank of Austria-Hungary
1889	87	246	60	26
1899	141	361	112	214
1909	151	633	159	267

But these huge amounts of gold are only to be regarded *technically* and not *economically* as mere hoards. Technically and economically they are two very different things, just like labour as a creator of value and labour as a creator of use value; a distinction of the greatest importance which Marx discovered but which up to the present has had no influence on bourgeois economy.

Money as gold technically remains in the bank vaults. But economically it circulates in the market in the form of instructions on gold, in the notes which the bank issues. The gold pieces function in the form of notes as circulating money, indeed the amount of circulating money in the form of banknotes is much greater than the amount of the money metal in the bank.

The report of the American Director of the Mint gives the following figures for 31 December 1910, in millions of dollars:

	Bank of England	Bank of France	Bank of Germany	Bank of Austria-Hungary
Amount of gold	151	633	159	267
Circulating banknotes	241	1024	391	477

The same report estimates the amount of gold in the great [central] banks of Europe on 31 December 1910 at 2,464 million dollars and the amount of circulating banknotes issued by them at 4,325 million.

The significance of the banknote is first of all of a technical nature: it reduces the need to transport large amounts of money. Furthermore it brings about a saving, insofar as the gold

coins lying in the bank's vaults are protected from the wear and tear of circulation. But in addition to these technical effects, the banknote also has economic effects. People do not see from a banknote whether it is covered by gold or not.

The bank may issue notes representing much more money than its gold hoard amounts to. So long as they are accepted as full representatives of the amount of money which they claim to represent, they fulfil the same functions and exert the same economic effects as real gold. The gold hoard in the banks therefore essentially serves only as a reserve fund for different purposes.

Marx identified as such functions the following:

> (i) a reserve fund for international payments, i.e. a reserve fund of world money; (ii) a reserve fund for the alternately expanding and contracting domestic metal circulation; (iii) (and this is connected with the banking function and has nothing to do with the function of money as simple money) a reserve fund for the payment of deposits and the convertibility of notes.[172]

The gold hoards of the great central banks thus have entirely different effects than the private hoards which we have previously considered. The latter diminished the amount of money in circulation, while the hoards in the banks increase it. To be sure, the bank hoards accumulate ever more strongly with the development of the capitalist mode of production, but the economic effect of the increasing gold production is not thereby lessened, but rather is immensely increased. The larger the bank hoard, all the more money there is generally speaking in circulation.

Just as little as the other factors considered here does banking show tendencies tending to weaken the effects of the growing gold production. To the contrary. It is true that the extent and conditions of gold production are not alone in determining the degree of influence of the economic effects of additional money. But all factors which next to gold production are decisive for it – the speed of commodity circulation, the industrial employment of gold as well as its division between hoard and circulating money, finally the introduction of substitutes for gold in the different functions of money and the credit system – have all developed in the last twenty years in such a way that they did not weaken but strengthened the influence of the increasing gold production on economic life and commodity prices.

[172]Marx 1981, pp. 701–2.

4. The rise in prices and misery

We have seen that the view that changes in the conditions of production of gold cannot under any circumstances bring about changes in commodity prices is already untenable for the reason that changes of this kind have already been observed.

We have further described the process by which the law of value operates in the case of gold. The mode of operation is simply this, that given a stable distribution of labour power in the different spheres of production, increased gold production creates increased demand for commodities and consequently causes a rise in prices. Only when the change in prices thus produced is not enough to enforce the law of value for gold, and when its production under capitalist conditions yields an extra profit for a considerable length of time, does the tendency towards the equalisation of the rates of profit manifest itself as a regulating element, which brings more capital and more labour into gold mining until the equality of the profit rate is restored – a law which is somewhat modified by the distinctive lottery character of gold mining, which always tends to keep the rate of profit in this industry below the average.

The rise in commodity prices caused by the increase in gold production may under certain circumstances be so large that the value of gold is not fully realised in exchange. If the limits that the above-mentioned lottery character imposes on gold production are overstepped, then the least productive mines will not only yield no ground rent, but they will also no longer yield enough profit to keep capital in operation. Then some of the mines will be abandoned and capital will leave gold production until an equalisation of the profit rates takes place.

The assertion of the law of value for gold must not under all circumstances be accompanied by capital movements, and a rise in [commodity] prices as a consequence of improvements in gold production or the discovery of richer gold fields may even have as a consequence a movement of capital into gold mining.

Varga is wrong, therefore, when he says that the present rise in prices cannot be the result of the changes in gold production because the capital movements effected by them are quite unimportant in relative terms.

The *theoretical possibility,* that the present rise in prices is connected with the increased gold production, seems to me undeniable. Another question is whether the possibility has become a reality. This cannot be proved in figures with the present state of statistics. But all the indications point out in that direction. I assumed when I began to investigate the

question of the rise in prices that the probabilities were in favour of gold being also partly responsible for the rise in prices. Varga's objections, however, made me to examine the question in more detail, and the more I did so, the more I became convinced that changes in gold production had contributed to the rise in prices. It would be a real miracle if these changes had had no influence.

But this does not mean, and I have certainly never maintained, that gold is the *only* cause of the rise in prices.

The whole economic life of capitalism is reflected in the movement of prices. All its criss-crossing tendencies, which sometimes obstruct and sometimes further each other, have an impact on price formation. One can and must, for scientific purposes, trace and investigate each one of the tendencies separately. In answering the question of the reason for the formation of certain prices, one must however seek to present an overall picture of all these tendencies.

Neither the rise in prices of the last two decades, nor the fall in prices of the two preceding decades since 1873, would have been so strong if changes in gold production alone were responsible for it. In the one case, as in the other, this factor was boosted to a great degree by others working in the same direction. To treat those other factors here in more detail would imply an unreasonable extension of the investigation and would be of little use, as they have been already sufficiently considered by different writers, including myself, on different occasions, so that we would be able to advance nothing new here. A few short remarks in this regard may therefore suffice.

To the factors that caused prices to fall after 1873 there belonged, in addition to the stagnation in gold production, the improvements of the transportation system, particularly the development of the trans-oceanic steamships and the building of railroads in America and Russia, by which great stretches of land previously scarcely or entirely unexploited, to a large extent still free from private ownership, came into the closest relationship with countries where capitalist production was highly developed. This caused a fall in the costs of production of foodstuffs and raw materials and thus a fall in their prices, which was in its turn reflected in the prices of industrial products.

But the same improvements in the means of transportation also brought into intimate connection those lands where, under the spur of increased gold production since 1851, capitalist industry had enormously extended its forces of production in two decades – England, France, Germany and the East of the United States. The wildest industrial competition broke out among them after the crisis of 1873, which at times reduced prices

below the cost of production.

The industrial states, with the exception of England, in order to meet this situation since the end of the 1870s and in the course of the 1880s, turned to the limitation of competition, at least foreign competition, by means of protective tariffs. Germany turned to protectionism in 1879, and from then on it has increasingly sharpened its protectionist policy from time to time. France followed in 1891. In the United States there was after 1870 an anti-tariff tendency, but a backward movement began in 1875, which finally reached a ruthless expression with the McKinley tariff in 1890.

But a protective tariff, although it may momentarily raise prices and hold them constantly higher than they would be without it, cannot abolish the depressing effect of a whole decade of falling prices on the world market. So the industrial capitalists sought a more effective means of abolishing competition among themselves and of transforming falling into rising prices, through the creation of *private monopolies*, through cartels, syndicates, trusts. At the outset this was chiefly with respect to areas whose monopoly character is aided by nature, such as petroleum, but particularly coal and iron, the life sources of modern industry.

These entities appeared in the 1880s, but first attained economic importance in the 1890s, and then quickly started from the beginning of the twentieth century to gain control over the whole production process.

At the same time the causes which had reduced the costs of production in agriculture ceased to operate, so that also for its products a rise in prices occurred, after the various capitalistic countries, with the exception of England, already had introduced protective tariffs for agricultural products simultaneously with the protective tariffs for industrial products, thereby bringing about a rise in prices in their areas above those of the world market.

The virgin soil of the newly-opened territory was, under capitalist conditions, rapidly exhausted by reckless farming; to maintain its old fertility or even to increase it now requires tremendous expenditure.

Above all is the fact that in our century the freedom from pressure of private property as it existed in American agriculture, which through its competition reduced European ground rent, came to an end. Also in America every land has its landlord, and can only be cultivated if it pays ground rent – that is, if the prices of the agricultural products are sufficiently high. Ground rent, an effect of higher prices of agricultural products, grows and becomes itself a cause of an additional rise in those prices. Because, although ground rent is surplus value, a portion of the excess of the price over the cost of production, for the agriculturalist it belongs to his costs of production. The higher the ground rent, the more from the income derived

from his harvest or his cattle he must hand over to the land- or money-owner, who is of no use to agriculture, instead of accumulating it as capital for the improvement and extension of his business. This manifestly happens today where the agriculturalist is a leaseholder. But he also feels it where he has to buy his land. Every change in possession increases the burden of agriculture so much the more, the higher the prices of agricultural products, and accordingly ground rent. And the more ground rent rises, the more the landowner turns into a land speculator, the more easily he sells his possession, the more often does land changes hands. All these causes of the rise in prices are still joined by the new great impetus that the arms race of the great powers receives through world policy [*Weltpolitik*: imperialism], which adds the increase in naval armaments to the increase in land armaments. Naval armaments takes place less through the increase in the number of combatants than by the growth and development of the technical apparatus, which knows no limits and proceeds more rapidly than the growth of the land army. Therewith also is boundlessly increased the waste of productive forces, which the states here literally throw into the sea, and the burdens on the people, which appear in the form of a steady increase in indirect taxation, and in a rise of the prices of all the articles of consumption of the masses.

The price-raising effects of gold production are enormously increased by all of these factors. We should not however believe that each of these factors, because it raises prices, also influences in the same way economic life as the others. A rise in prices can come from two causes: an increase of demand or a diminution of supply.

We have seen how an increase in demand, i.e. in the demand of the money owners, operates. It signifies more active production, more active circulation, increased prosperity. Under these conditions, everybody gladly puts up with a rise in commodity prices. If prices and wages rise in the same proportion and if they apparently do not change their mutual relations, the condition of the worker is improved as a consequence of the more rapid turnover of capital, because of the greater steadiness of employment, which increases the annual sum of his wages more than the rise in commodity prices.

At the same time, the capitalist also wins, because due to the rapid turnover of capital the annual sum of his profits increases considerably; he can not only consume more, but also accumulate more.

So it seems that high prices are synonymous with economic prosperity, and that the economic task of the state is to ensure increasing prices – which indeed, as we have just seen, it most earnestly tries to do by means of protective duties and indirect taxation.

But there are different kinds of high prices. A rise in prices has a different effect where it does

not spring from an increase in demand but from a reduction in supply, for instance as a result of bad harvests. In this case, the farmer charges a higher price per hundredweight, but in exchange the number of hundredweights that he puts on the market is reduced. His total income does not grow, but he and his labourers now have to pay more for flour and bread. He and his people have less money left over to acquire industrial products than they formerly did. The same is true of the rest of the population. The demand for industrial products is not increased, indeed it often diminishes, while the cost of living of the workers rises, so that they must strive for an increase in wages; likewise there is a tendency to a rise in the prices of raw materials, which increases the drive towards a rise in the prices of manufactured products, while the demand for them declines, as we have seen. This rise in prices, if it takes place, must cripple still further the already reduced sales of commodities and therefore the turnover of capital; if it does not take place, the prices of the manufactured products remain behind the increased costs of production. In both cases, the profit rate sinks, and the consequence is a general stagnation and misery among the great masses of workers.

Finally, international competition is still to be considered when analysing the question of the economic effect of a universal rise or decline in prices. On the world market, that nation asserts itself soonest which sells cheapest, and this can only be done continually and successfully if it has the lowest production costs.

Hence the praise for low prices sung by the school of free trade. This is not false; it has, however, not an absolute but only a relative justification. But the absolute glorification of high prices beloved by the protectionists is still less justifiable. Only under very peculiar conditions are higher prices synonymous with economic prosperity. Among those conditions does not belong the burdening of an industry working for the world market with high state taxes, such as a system of protective tariffs for all products, including raw materials and foodstuffs, represents.

Generally, it may be said that a rise in prices which springs from an increase in demand is linked to effects which signify heightened prosperity and that, on the other hand, a rise in prices caused by a reduction or obstruction of supply heightens misery.

The consequences of increased gold production on social conditions therefore mean the exact opposite of the consequences of the other price-raising factors here considered. Moreover these factors are not all simultaneously active in the same proportion. Depending on whether one or the other of them predominates, social life takes a different character; the price increase can be welcomed as a sign of prosperity, or detested as an agonising experience, as a state of calamity.

Since 1894 and until a few years ago predominated the effects of gold production that made themselves felt earlier and more powerfully than the other price-raising factors—with the exception of the protective tariffs, which only operated in a transitory fashion. Under these conditions, there arose that view which we call revisionism; the theory that the capitalist mode of production develops tendencies which continually improve the condition of the proletariat, limits its exploitation, and thus lead to a gradual overcoming of all the tendencies to immiseration without any political revolution. Just as in the sixteenth century the force of Protestantism in Germany, and after 1848 of Chartism in England, so the revolutionary drive of the entire working class was weakened through the increased gold production. But only briefly on this occasion.

The developments of the last years have abruptly dashed the expectations of revisionism. Do the revisionists have the chance of ever finding again a favourable ground?

The answer to this question depends very closely on the expectations which we may entertain of gold production.

The speed of its growth since 1890 may be found in the following table:

Year	Gold Production in thousand kilogrammes	Addition over former years	
		Absolute in thousand kilogrammes	Per cent
1890	179		
1891	196	17	9.4
1892	221	25	12.7
1893	237	16	7.2
1894	273	36	15.1
1895	299	26	9.6
1896	304	5	1.7
1897	355	51	16.7
1898	432	77	21.6
1899	462	30	6.8
1900	383	-79	-17.1
1901	393	10	2.6
1902	446	53	13.5
1903	493	47	10.5

1904	523	30	6
1905	568	45	8.7
1906	605	37	6.5
1907	621	16	2.6
1908	666	45	7.2
1909	683	17	2.5
1910	684	1	0.1
1911	703	19	2.8

It can be seen that from 1891 to 1905 the annual growth in gold production is significant, if we omit the time of the Boer War and its consequences (1899, 1900 and 1901). In 1897 and 1898 in particular the figures climbed rapidly owing to the discovery of the Alaska gold fields. But since 1905 the percentage of annual increase product has declined significantly, with the exception of 1908. In 1910 this increase in gold production was almost nil: 0,1 per cent.
The amount of gold yields of individual major areas of gold production is remarkable. It amounted to, in millions of dollars:[173]

Year	Africa	United States	Australia	Other countries
1890	10	33	30	41
1891	16	33	31	50
1892	24	33	34	55
1893	29	36	36	57
1894	40	40	42	60
1895	45	47	45	63
1896	45	53	44	61
1897	59	57	53	67
1898	80	64	65	77
1899	73	71	79	88
1900	9	79	73	94
1901	9	79	77	99
1902	39	80	82	96
1903	68	74	89	97
1904	86	80	88	92
1905	113	88	86	93

[173]According to the American Director of the Mint; numbers for 1911 from a report of the *Engineering and Mining Journal*.

1906	135	94	82	90
1907	152	90	76	95
1908	167	95	73	108
1909	171	100	71	112
1910	175	96	65	118
1911	191	96	64	125

In Australia gold production has therefore already begun to decline; in 1903 it reached its highest point. Since then it has fallen from 89 to 64 million dollars.

In the United States gold production already appears to have reached its maximum. Since 1906 it has made only limited progress. The decline in 1910 in comparison with 1909 continued further in 1911. The precise figures amounted in 1909 to 99,673,400 dollars; in 1910 to 96,269,100 dollars, and in 1911 to 96,233,000 dollars.

In South Africa, gold production still makes enormous strides; this, however, should not be attributed to the expansion of the gold districts, but to a stronger exploitation of the existing ones, which must consequently be all the more rapidly exhausted.

The Director of the Mint[174] quotes a Johannesburg correspondent of the *Engineering and Mining Journal*, who says

> One is now in a position to judge what the year 1911 has meant in the history of Rand mining. It seems that the best of the profitable ore on the Rand is exhausted and that the mining industry will have reached its maximum output in a few years and has already nearly reached the maximum of profit, if it has not already passed it. A few years will see many well-known outcrop producers exhausted, such as the Jubilee, Salisbury, and the Champ d'Or, which failed this year.

So there remains only the gold of 'other countries', particularly Canada, India, Mexico, and Russia. For Russia the *Engineering and Mining Journal* reports a reduction in production from 43.2 million dollars in 1910 to 40.6 million dollars in 1911, for Mexico from 24.1 to 19.5 million, for India from 12.1 to 10.5 million, for Canada a slight increase from 10.2 to 10.6 million dollars. In the meantime the gold production of the most important district of Canada, the Yukon district, has been losing its earlier significance for years already. Gold production in the Yukon district has been, in millions of dollars since 1896:

1896	0.3	1904	10.5

[174]Roberts 1912, p. 67.

1897	2.5	1905	7.9
1898	10	1906	5.6
1899	16	1907	3.2
1900	22.3	1908	3.6
1901	18	1909	3.9
1902	14.5	1910	4.6
1903	12.3		

Of course the exhaustion of the hitherto-known gold fields of the world, in the sense that they will yield absolutely no more gold profitably, is not to be expected soon. But it is just as little to be expected that a continuation of the rapid increase in gold production, at the rate at which it grew from 1892 to 1905, will be maintained. It is of course not impossible that gold fields as rich as those in South Africa will be discovered once more, but the probability of that taking place is increasingly smaller.

Gold has, within the realm of commodity production, from time immemorial so aroused the greed of people, that it was always sought with the greatest eagerness. The discovery of new gold fields no longer occurs in lands of developed civilisation but only in the wilderness, newly-discovered and for the first time accessible; at first, in the sixteenth century, in Spanish America, then in Brazil, where in 1680 rich mines were opened in Minas Gerais. In Russia, gold was found in the Ural Mountains in 1743, the opening of Siberia at the beginning of the nineteenth century made known the existence of gold fields there. In the middle of the nineteenth century followed, as we have already said, the discoveries in California and Australia, and at the end of the nineteenth century those in South Africa and Alaska: it is always, as we see, uncultivated districts in which new gold fields are found. But capitalist civilisation continually extends throughout the world; with giant strides it opens one place after another. Undiscovered lands capable of yielding gold become scarcer year by year. The number of places capable of surprising by new extraordinary gold discoveries, and of putting bankrupt capitalism on its feet again for a time by means of a new big hit, becomes always smaller.

There exists a second possibility for a further expansion of gold production: through extraordinary technical advances, which would render possible the exploitation of already-known gold fields with the expenditure of less labour than was hitherto feasible, or the extraction of a greater amount of product with the same labour expenditure. The possibility of such advances is undeniable, even very probable in our times of unbroken technical

revolution. But nothing justifies the assumption that this advance will proceed more rapidly in mining than in other branches of production, and that it will counteract the increasing difficulty of getting gold (resulting from the exhaustion of the upper strata and the necessity of going ever deeper) to such an extent that the rate of increase in gold production observed on average during the last two decades will continue. And that is the point: for gold production to operate as a means of advancing prosperity, it is not enough that it should continue merely in the same degree as at present, or even in a lessened degree. It must rather grow uninterruptedly.

The capitalist mode of production itself develops the compulsion, the necessity not only of a *constant* but also of an *increasingly rapid* expansion, because the accumulation of capital increases from year to year and, at the same time, technology continually expands the volume of the product yielded by a given amount of labour power. However, the sale of this mass of products, which grows enormously both through the increased productivity of labour as well as through the increase in capital, its consumption and the continuation of production on an ever expanded scale, and therewith social prosperity, depend under the rule of commodity production on the increase of these factors confronting an equally increased demand – that is to say, all other conditions being equal, on an [equally] increased mass of money.

Now this is admittedly true only when all other conditions are equal. These may change and make the mass of gold now more, now less economically effective.

But there is no ground to assume that they can counteract the slowdown in the growth of gold production. The quicker or slower circulation of money is closely connected with the general course of the production process; it increases in times of prosperity and diminishes in times of crisis. Nothing justifies the expectation that a falling gold production will coincide with increasing prosperity and that less additional gold will have a greater effect due to a more rapid circulation.

It may be possible that in the Orient, particularly in Egypt, India and China, there is still much hoarded gold, which by the advance of capitalism, particularly of the banking system, might be turned into circulating, demand-generating money.

We have already seen how the Orient, since the close of classic antiquity, has attracted more and more gold and silver, which has been withdrawn from circulation and hoarded. These treasures have been plundered from time to time, but its foreign trade, which exports far more value than it imports, let such treasures accumulate ever anew there.

The *Bulletin de la statistique générale de la France* in its July number gives a table which

shows well the economic role of India.

Foreign trade of British India, annual average in millions of francs:

Year	Goods			Precious Metals		Excess of export
	Imports	Exports	Balance of exports	Gold import (in excess over export)	Silver	
1835-1839	118	264	146	together 50		96
1840-1844	183	328	145	" 55		90
1845-1849	217	273	156	" 42		114
1850-1854	263	453	190	27	63	100
1855-1859	371	593	222	60	187	-25[175]
1860-1864	571	1003	432	140	242	50
1865-1869	754	1330	576	139	237	200
1870-1874	786	1339	553	73	86	94
1875-1879	843	1324	481	15	140	326
1880-1884	1035	1631	596	85	128	383
1885-1889	1138	1682	504	58	165	281
1890-1894	1200	1779	579	39	206	334
1895-1899	1121	2635	514	38	95	381
1900-1904	1423	2099	676	104[176]	138	434
1905-1909	2015	2782	767	157	284	326
1910	2062	3158	1096	365	159	572
1911	2248	3519	1271	403	146	722

According to the figures of the trade balance, India must be continually getting richer, since the excess of exports grows strongly and uninterruptedly. But the lion's share of this surplus goes to England, which offers nothing in return. So long as this surplus is not offset by the importation of precious metals, it coincides with the magnitude of the British exploitation of India. Despite all the nice speeches, this exploitation grows from year to year, impoverishing India.

And yet, despite that, India accumulates hoards of precious metals; it produces gold (17,826

[175]In these five years import exceptionally dominated. It was the beginning of the great railways construction.
[176]Since 1900 the gold currency has definitively been established in India, gold coins are there abundantly put into circulation. Previously silver currency prevailed. The gold import increases since then, the silver import decreases.

kilograms in 1910, or 2.2 million pounds), and it still imports precious metals to the amount of approximately 400 million marks. In a lecture before the East India Association, Sir James Wilson estimated the excess importation of gold in India since 1890 at five billions marks, a tenth of world gold production during that period of time.

Similar, if not so great, is the coincidence of the impoverishment of the popular masses and the collection of gold hoards in Egypt.

It is quite impossible to calculate or even to estimate how much of the imported gold is used for industrial purposes, how much remains or becomes coin and how much of it goes into circulation or is stored as treasure.

Table of Egyptian foreign trade, annual average in millions of francs:

Year	Goods	Goods	Goods	Precious Metals	Precious Metals	Excess of export
	Import	Export	Excess export	Gold import (in excess over export)	Silver import	
1890-1894	227	363	136	18	0	118
1895-1899	262	375	113	41	2	70
1900-1904	418	517	100	70	5	25
1905-1909	610	680	70	51	5	14
1909	569	737	168	14	0	154
1910	603	829	226	151	1	74

The custom of using precious metals for jewellery, or stockpiling them as hoards, is still strong in these countries. The director of the American Mint asked in 1909 the American Consul General in Cairo, what happened to the gold that went to Egypt. The Consul related that in 1905 the stamp bureau of Cairo had undertaken investigations in the gold bazaars which showed that in that year, gold to the value of two million pounds had been turned into jewellery. It is of course impossible to determine exactly how much of this was newly-imported gold and how much old material.

A few typical facts which the Earl of Cromer mentioned in 1907 in a speech in London are worth noting:

> But they deal with them in quite the traditional way. They secrete their gold just as their ancestors did four thousand years ago. In the cellar of one old man who died not long since were found £80,000 in specie. A farmer who bought some land for

> £25,000 sent the purchase -money loaded on a train of donkeys. He had dug it up from his garden where it had been lying hid! No bank for him. He preferred to keep his fortune under his own soil.[177]

It is clear that in the Orient large quantities of gold still lie dead, which could be brought into capitalist circulation. But this process would not begin just now; it has been already vigorously going on for the last two decades. If it is to offset the consequences of a diminished gold production, it must not only go further, but at a much more rapid rate than hitherto. Nothing suggests that we should expect that.

We must rather expect that also this process will slow down, because, as in the case of the unexplored areas of the earth that could till harbour gold fields, the places in the Orient still closed to capitalism, which could provide it with hitherto unused treasures, will also diminish from year to year, and will be more and more limited in proportion as the scope of the capitalist circulation process is extended and the quicker the railroads and banks are developed in the Orient.

Thus the increased gold production, and along with it the methods of increasing money production which partially work in parallel with it and partly depend upon it, are ceasing to deploy those economic effects which lead to a price increase. Therewith however the price increase does not come to an end. It proceeds further and is precisely first now becoming unpleasantly felt. For now the other above-mentioned price-raising factors step to the foreground, which become not weaker, but rather stronger.

We will now offer some figures in order to characterise the present rise in prices. They are taken from the price statistics of the American Labor Bureau in Washington.[178] As a basis of the price movement, the annual average for the years 1890 to 1899 is taken and set at 100. We first give the movement of the two great groups of raw commodities and manufactured commodities, then some subdivisions, which are particularly informing as regards price movement.

The table is as follows:

Year	Raw commodities	Manufactured commodities	Farm products	Cotton	Cloths and clothing	Metals and implements	Pine [white boards] lumber
1897	87.6	90.1	85.2	92.2	91.1	86.8	93.7

[177]Fyfe 1911, pp. 50–1. [Actually this is not a speech by Cromer but part of Hamilton Fyfe's narrative.]
[178]Bulletin of the United States Bureau of Labor Statistics, Wholesale prices 1890 to 1911.

1898	94	93.3	96.1	76.9	93.4	86.4	96.8
1899	105.9	100.7	100	84.7	96.7	114.7	107.9
1900	111.9	110.2	109.5	123.8	106.8	120.5	120.5
1901	111.4	107.8	116.9	111.1	101	111.9	119.4
1902	122.4	110.6	130.5	115.1	102	117.2	137.2
1903	122.7	111.5	118.8	144.7	106.6	117.6	141.9
1904	119.7	111.3	126.2	155.9	109.8	109.6	141.5
1905	121.2	114.6	124.2	123.1	112	122.5	150.7
1906	126.5	121.6	123.6	142	120	135.2	171.6
1907	133.4	128.6	137.1	153	126.7	143.4	187
1908	125.5	122.2	133.1	134.8	116.9	125.4	189
1909	136.8	123.9	153.1	156	119.6	124.8	194.4
1910	139.7	129.6	164.6	194.8	123.7	128.5	196.1
1911	139.9	126.6	162	168	119.6	119.4	201.9

Generally we can say that the prices of manufactured commodities fluctuate less than those of farm products, the harvest of which is so dependent on weather. However, it is striking that the tendency to a rise in prices is much stronger in farm products than in industrial products. And in the latter the tendency of prices to rise hardly manifested itself in the last years, the years of the slowdown of gold production. Manufactured commodities as a whole reached their highest point in 1907 with the figure 128.6, which they surpassed by a trivial margin in 1910 with the figure 129.6, only to descend in 1911 to 126.6. Besides that, cloths show the following figures: 1907, 126.7, 1911, 119.6; metals and implements for 1907, 143.4, and for 1911, 119.4. By contrast, we find in farm products, 1907, 137.1, 1911, 162.0. For cotton, 1908, 153.0, 1911, 168.0, after having climbed in 1910 to the incredible height of 194.8. Pine [lumber], however, climbs upward uninterruptedly. Even the crisis, which everywhere in the years 1907 to 1908 brought about a fall of prices, had no effect on the price of pine. Here appears most clearly the effect of the capitalist destruction of forests. In agriculture it is the price-raising influence of private property.

The general character of price developments since 1907 is this: steady rise in prices of the articles of consumption of the worker and of agricultural raw materials for industry, slower increase in the demand for industrial products, stagnation also in the wages of the industrial working class. This applies initially only for America. In Europe there are not such complete price statistics. But from what is known here on price statistics, the picture is the same.

And this development will progress, the more environmental pillage [*Raubwirtschaft*] continues, the more, with the addition to the population and the expansion of the area of capitalism, private property on land extends its realm and its burdens become more onerous. The cartels of industrial capitalists could paralyse the depressing effects of these factors for their profits, but this would press with double weight upon the non-cartelised entrepreneurs and upon the working class.

And the attempt to offset the rise in the price of agricultural raw materials, such as cotton and of the necessaries of life, by means of a policy of colonial conquest would be no less detrimental to the workers. Because its effects on agricultural production are remote and uncertain, and private property in land as well as environmental pillage would drive prices higher also in the colonies. Initially, however, colonial policy involves a strengthening of the tendency to a rise in prices, as the unavoidable consequence of the rapid increase in naval armaments and thus in taxes, which mean a new burden on the working class.

The rise in prices now completely changes its character. As long as the influence of augmented gold production, augmented demand dominated the process, it was largely welcomed as an accompanying phenomenon of growing prosperity. Since the influence of augmented gold production has receded and the other factors of the price increase asserted themselves, which do not have the effect of an augmented demand but of a reduction in supply, this rise in prices assumes an ever more tormenting character. From a phenomenon accompanying prosperity, it becomes a cause of growing misery, and besides no longer merely social, relative misery, increased exploitation, but also absolute, physical misery.

The constant rise in the prices of the necessaries of life will be accompanied, as the new tendencies gain momentum, by a growing permanent unemployment, [and] therewith the complete unleashing and greatest intensification of those tendencies of the modern mode of production, to which the Erfurt Program refers with the words of Marx's *Capital*:

> the mass of misery, oppression, slavery, degradation and exploitation grows; but with this there also grows the revolt of the working class, a class constantly increasing in numbers, and trained, united and organized by the very mechanism of the capitalist process of production.[179]

The class struggle of the proletariat always continues, with rising or sinking prices, in times of growing prosperity as well as in those of growing need, because it arises from class

[179]Marx 1976, p. 929.

antagonisms that are generated by capitalist society under all circumstances. But the forms of the class struggle are different during times of industrial upswing than during economic stagnation. The former strengthens the organisations of the proletariat, its sense of force and its power, but it blunts the spur of class antagonisms and weakens the revolutionary drive towards the overthrow of the whole capitalist system and the state power which protects it.
The period of stagnation or increasing misery sharpens the spur of class antagonism and strengthens the revolutionary drive of the proletariat as conditions become more unbearable.
Such times therefore always lead to profound disturbances of the existing state- and social order. But from them the proletariat may be able to derive all the greater advantages, it may by them be able to conquer all the sooner new positions of power in the state as against the property-owning classes, the more purposefully it used the preceding period of upswing to increase its means of power and its class consciousness.
A look back over the last two decades gives us the conviction that the party and the unions have done their duty. So we may confidently face the struggles which the new era of capitalism has in store for us, in which no rapid increase in gold production can any longer interfere with the sharpening of class antagonisms, in which capital will bring about its growing enrichment only through the growing impoverishment of the popular masses, increasingly forcing them, on pain of their own destruction, to bring about the destruction of the capitalist system.

Chapter Twelve

Gold Production and the Rise in Prices[180]

(5 March 1913)

Anton Pannekoek

Antonie (Anton) Pannekoek (1873-1960) was a Dutch Marxist active also in the left German Social Democratic movement (from 1899 until 1914) and, after a Communist interlude, in the councilist movement (after 1921). An astronomer by profession, Pannekoek published in Dutch in *De Nieuwe Tijd* and in *Het Volk*, and in German in *Die neue Zeit* and the *Leipziger Volkszeitung*. In 1906 he was appointed teacher at the SPD party school in Berlin, but could not continue his activities because of a ban by the authorities in September 1907. For a time he worked at the German party archives and finally published a *Zeitungskorrespondenz* (1 February 1908 – 1 July 1914) with articles for German Social-Democratic newspapers which subscribed to it. Working from Berlin and later from Bremen, Pannekoek wrote also for *The International Socialist Review*, edited in Chicago by the left of the Socialist Party of America, from 1906 on. From April 1910 Pannekoek worked as party lecturer in Bremen, where he gave courses and wrote articles for the *Bremer Bürger-Zeitung*. The first year he was paid by the party and trade union movement in Bremen, then only by the party department, because the leftist position of Pannekoek aroused antagonism among the union bureaucracy. He travelled through southern Germany and Switzerland holding lectures for the party regionals. As member of the SPD, he attended the party congresses at Essen (1907), Jena (1911), Chemnitz (1912) and Jena (1913). When the split between the Kautskyist centre and the SPD left led by Rosa Luxemburg took place in 1910, Pannekoek aligned with the left, supporting Luxemburg's positions on the mass strike and parliamentarism against Kautsky's increasing reformism, while at the same time retaining his admiration for him as an economist until their break after 1913, when Pannekoek would no longer publish in *Die neue Zeit*. From a distance he also gave advice to his friends in the Netherlands, who in 1907 founded the magazine *De Tribune*, which attacked the revisionist leadership of the SDAP. When Troelstra and other SDAP leaders removed David Wijnkoop and his associates from the party ranks in 1909, Pannekoek supported them in founding the *Sociaaldemokratische Partij* (S.D.P.)—which later became the Communist Party of Holland—and worked

[180]Pannekoek 1913a.

closely together with Herman Gorter and Henriette Roland-Holst.

Pannekoek's 1910 article 'Gold as Source of Misery' attributed the rise in prices since 1896 largely to a fall in gold's value (Pannekoek 1910). He spent some time writing a polemic against Hilferding's theory of money, but abandoned it after he saw Kautsky's response, which 'in a much more thorough fashion raised the same objections against it that I did' (1912 letter to Kautsky). In the present article Pannekoek gives an overview of the debate in *Die neue Zeit* as well as a review of the brochures of Kautsky (the previous item in our collection) and Karski that just had appeared. The Polish Marxist Balthasar Machlewski ('Karski'), wrote weekly economic reports, paying attention to the details of price movements in particular products. Karski stated his position on the influence of gold production on commodity prices in the *Leipziger Volkszeitung* already in 1911 (Karski 1911). We have not included in this anthology his brochure *Inflation, Commodity Prices and Gold Production* (Karski 1913b), or his rather acrimonious exchange with Pannekoek in the *Leipziger Volkszeitung* after the publication of this article (Karski 1913c, Pannekoek 1913d, Karski 1913d).

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I.

For many years the ever-growing rise in prices has constituted the worst inconvenience for the working class, and it is therefore one of the preeminent questions requiring the attention of the struggling proletariat. Statistics show that since 1896 the prices of all commodities have grown constantly. Taking as a basis the prices for the years 1894–96, they had grown in Germany by the year 1900 by approximately 25 per cent. After a temporary reduction, they reached in 1907 a level 40 per cent higher than that of 1894–96, and after a similarly short decrease, prices again increased significantly beyond that level in 1911 and 1912. At first this rise in prices was not felt to be too oppressive, because at the same time the employment opportunities improved due to the favourable economic conjuncture, and the powerfully emerging trade unions more than made up for the rise in the prices of the articles of consumption through significant wage increases in the decade until 1905. But since then, it has become increasingly more difficult for wages to keep up with inflation. The employers' associations have been strongly strengthened and strive to prevent every struggle with lockout threats. Many groups of workers have experienced an outright decline in their real wages. The rise in prices oppresses more and more the working class.

It is therefore only natural that the question as to the causes of this rise in prices should awaken the highest interest. It partially finds an answer in the tariff policy of the German Reich. Through the usury tariff of 1902, the prices of the most important articles of consumption were greatly increased; for that reason, the rise in prices is here much stronger than in England. For this the workers must than their 'friends', the National Liberals and the politicians of the Centre Party, who helped the Junkers push through those import duties, and their beloved brothers in the Block, the Progressives [*Freisinnigen*], who did not lift a finger to prevent their introduction. All these friends of the people are already preparing to increase the tariffs once more in a few years.

But in addition to this usury tariff, part and parcel of the utterly reactionary German policy, there are other circumstances which have their origin in the world economy. Because free-trade England also witnesses a rise in prices, although less pronounced than here. Since 1896, prices in England (according to the average published in the so-called index number) rose by approximately 13 per cent by 1900 and by about 23 per cent by 1910. In order to order to explain this increase, one must go back to causes lying in the general nature of modern capitalist development. Among such causes come into consideration, for the raw materials and articles of consumption, the lack of virgin lands not yet burdened with ground rent (the massive cultivation of cereals on such lands in America brought about the fall in cereal prices from 1875 to 1896) and the growing industrialisation of the agrarian countries; and for all other commodities, including the industrial products, the cartels and trusts, which artificially raise prices because of their monopoly, and the fall in the value of gold.

While most of the causes of the rise in prices are obviously clear and distinctive, strong differences of opinion have arisen over the last-mentioned cause. The simplicity of the explanation has led theorists and economists, in particular, to stress that cause. The price of a commodity is not something that depends just on its conditions of production; its price shows how much gold is given in exchange for that commodity, and if gold production costs less labour, more gold must be given [in exchange] for that commodity, as long as it costs the same amount of labour to produce it. If a reduction in the amount labour required for gold production takes place, it will manifest itself in a general increase in prices.

This whole argumentation is regarded, particularly in the petty-bourgeois circles of America, simply as a subterfuge of the great trusts, at whose service bourgeois science is, to divert attention from their own predatory policy and to falsely present their plundering of the public through high prices as an unalterable effect of general economic laws. However, one would look in vain in their writings for any evidence of the falseness of those theoretical

arguments; what those circles have to offer are only superficial day-to-day politics without any deeper insight. It is also clear that bourgeois economics is incapable of offering a thorough treatment of this question. It was first given such treatment when the same differences of opinion appeared in the ranks of Social Democracy.

Among Social Democrats, for whom the Marxist theory of value has become part of their own flesh and blood, the view generally prevails that improvements in gold production played a significant role as one of the causes of the modern rise in prices. Already the fact that this rise in prices coincided with a period in which the world production of gold grew enormously, mainly through the rich Transvaal mines, points to this fact. While the world production of gold from 1850 (when the Californian gold mines were discovered) to 1890 stood at approximately 200,000 kg annually, it increased rapidly from then on. In 1890 it was already more than 400,000 kg annually, and in 1911 it reached the amount of 700,000 kg annually. This rapid growth points to the fact that the amount of labour contained in one kilogramme of gold must have sunk, and this fact must have manifested itself in a general increase in prices. Therefore gold production was listed amount the causes of the current distress in the excellent brochure of comrade Otto Bauer, *Die Teuerung* [*The Rise in Prices*] (Varga 1910). This view was opposed a year and a half ago by the Hungarian comrade Varga in an article in *Die neue Zeit*, where he stated that technical improvements in gold production could never lead to a general rise in prices. This gave rise to an interesting and learned discussion, which took place mainly on the pages of *Die neue Zeit*. Since that discussion has now reached, so to speak, its conclusion in two special brochures, one by Kautsky, which appeared as a supplementary issue of in *Die neue Zeit*, and the other by Karski, it is appropriate to summarise here the general course of that debate as well as its results, particularly because it has actually enriched our understanding in new, unexpected and valuable ways.

Varga's argumentation is as follows. Everywhere in the world there is gold, for instance in the waters of the oceans. But everywhere it is present in such small quantities, that to extract it would require far too much expenditure of human labour or excessively high costs. Its extraction is profitable only where it occurs in large quantities, that is, in gold-rich rocks. Since out of one kilogramme of gold 379 coins of ten marks can be coined, the exploitation of a mine only yields a profit if the production of one kilogramme of gold costs less than 3,790 marks. What happens if a better production method is found, for instance a new procedure, like the mining of gold with the help of cyanide introduced in 1890? Then in an old mine where previously, let us say, 2,500 marks had to be spent to extract one kilogramme of gold,

this expenditure fell to, let us say, 2,200 marks, and profits grew accordingly. A series of gold mines with ores which previously were not exploitable because of their low gold content were brought into operation, because only then they began to yield a profit. In them, the extraction of one kilogramme of gold still cost the old [labour] expenditure; for the mines that just began to yield a profit, the costs of gold production were as high as they were before [the introduction of the new production method], and the only difference was that, as a consequence of the better procedure, these [i.e. the least profitable] mines were poorer in gold than before. For the products of agriculture, which cannot be increased at will (as opposed to the industrial products), the rule applies that those produced under the worst conditions determine the price, and that all the producers who can produce under more favourable conditions, and therefore at a lower price, but nevertheless also fetch that high price, make as a result an extra profit, a ground rent. Thus, for instance, in cereal production: if not enough lands are brought into cultivation, the price rises so much as a consequence of demand, that the cultivation of as much worse land becomes profitable as must be added to in order to cover that demand. This worst land determines the price and all the other cereal cultivators make an extra profit. For the same reason, the worst mine, only just brought into operation, determines the price and therefore, in the case of gold, the exchange rate with the other commodities, which manifests itself in their prices. Despite the better procedure, despite the higher productivity of labour, [according to Varga] this exchange rate between gold and commodities has not changed. Changes in gold production cannot therefore be one of the causes of the rise in prices.

How is such a result, which seems to be a slap in the face of the foundations of political economy, possible? [According to Varga,] that is simply because in gold production there is no competition. In all other branches of production, a reduction in the costs of production causes a fall in prices, because the producers compete with each other, trying to dispose of their commodities in a mutual contest, and in order to do that they must lower their prices as much as their profits allow them [i.e. until they reach the average rate of profit]. But gold producers are not plagued by this worry. Whoever has gold, can immediately exchange each kilogramme for 2,790 marks in gold coins at the [central] bank, and in return he can buy whatever he wants. Therefore, for gold the force which in other commodities ensures that they will finally be exchanged according to their real production costs is absent. Therefore, [according to Varga,] whoever claims that changes in the technique of gold production can cause a general rise in prices, has the obligation to show the mechanism which brings about that price increase.

II.

Varga's argumentation that improvements in gold production cannot be a cause of the rise in prices is very strange, as was pointed out in an article in *Die neue Zeit* signed with the initials J. v. G. Then came to Varga's help comrade Hilferding, who indeed outsmarted him. Hilferding took as his starting point a theory of money which had its origin in the phenomena of the Austrian paper currency. Given the fact that the [central] banks absorb all the gold offered to them, in order to pile it up in their vaults, and only bring as much money or paper into circulation as required by commodity circulation (so that the overproduction of gold does not manifest itself in circulation), as well as the fact that money and commodities can only determine their mutual exchange rate when they actually face each other in the marketplace, Hilferding concludes that the labour-value of gold can have no influence on commodity prices. [According to Hilferding,] in gold we have a fixed measure of value, which through a historical development reached a certain exchange rate with the commodities and has been kept in that ratio through the state decreed [*staatlich verordnete*] gold currency. Hilferding claims that this exchange rate now remains completely unaffected by all changes in the productivity of labour in gold extraction. This astonishing theory was soon cut to pieces so thoroughly by Kautsky that it slid out of the discussion. Even if the [central] banks absorb all the gold, they must give in exchange for it coins or paper money, which in one way or another are employed by their owners for the purchase of commodities. So, only Varga's argumentation remains. But already practice had demonstrated that it must be false in some way, a proof that can be found in Karski's and particularly Kautsky's brochure. Because, as a matter of fact, a powerful rise in prices has already happened once, which must be traced back directly to gold production. When, after the discovery of America, the masses of gold and silver accumulated there were easily robbed and sent to Europe, they brought about here such a strong rise of commodity prices that the exploitation of the European mines in Saxony, Bohemia and Styria was no longer profitable – a fact that had a great influence on Germany's internal political developments. It was not the production costs in Germany that determined the value of gold, which should have been the case if Varga's views were right. Europe ceased to be a centre of production of precious metals, and something similar happened with cereals [three centuries later]. While [Ricardian ground rent] theory assumed that with growing needs ever poorer lands would be brought into

cultivation, which would cause agricultural prices to rise, in practice suddenly huge quantities of American cereals, cultivated in fertile soil, appeared on the European market, driving their prices down and making the cultivation of cereals in Europe itself unprofitable. It was therefore obvious from these practical examples that Varga's thesis had to be incorrect, but it was now essential to detect the mechanism by which changes in gold production impacted on commodity prices.

This task was undertaken by Otto Bauer in *Die neue Zeit* (April 1912). [According to Bauer,] it is certainly correct that gold producers do not have to compete with each other. But there is still another way for competition to operate. If a technical improvement is introduced in some branch of production, given constant prices profit will considerably increase in it. The competition between producers within that branch then brings about in a fall prices and also in profits. This competition may not be strong enough to reduce prices to such an extent that profits in this branch of production will fall until they reach the average rate of profit. Can those producers always count on their unusually high profits? No, because here a second force appears: competition between capitals. Capitals always look for investment opportunities where the greatest profits are to be made, and withdraw from the branches with low profits. In the branches with high profits production is expanded, and an overproduction develops which brings down prices, until also in them the average rate of profit is reached, while, on the contrary, in the other branches with a lower-than-average profit rate, profit grows through the reduction of production. Thus the competition between capitals causes the rates of profit in the different production branches to be always equalised. Bauer applies this fact to gold production. The first form of competition, the competition within the production branch, may here be lacking, but the second, the competition between capitals, operates also here. An improvement in production methods which increases profits lures more capitals into gold production and takes them away from other production branches. Gold production increases, and with it the demand for workers, machines and articles of consumption, while commodity production does not expand, or does not do it as much as would otherwise have been the case, and commodity supply becomes insufficient. Therefore commodity prices must increase, first for the commodities consumed in gold extraction, by gold capitalists and workers. This rise in commodity prices means a general rise in profits, a growth of demand, of the spirit of enterprise, which gradually extends to the whole economic system and drives prices up. In this way, also the production costs for gold industry increase and its profit rate sinks until it reaches the average. The immediate cause of the general rise in prices therefore lies [according to Otto Bauer] in the fact that too big a

share of the new capitals flew into gold production, instead of being invested in the production of useful objects.

> That in the world economy such a big part of social labour is not directed to the production of use values but to the production of the measure of exchange values [i.e. of gold] belongs to the *faux frais*, the *incidental operating expenditures* of the capitalist mode of production. We must pay these *faux frais* of capitalism by buying the commodities more expensively. The larger the part of social labour dedicated to gold extraction, the more oppressive the rise in prices is. (Otto Bauer, "Gold Production and the Rise in Prices", 1912)

Bauer's argumentation was opposed by Varga in *Die neue Zeit* as well as by Karski in his above-mentioned brochure. Both pointed out that the share of gold production, and of the capitals invested in it, in total production is so small, that one cannot speak about a withdrawal of capital from other production branches. They argued that, whether one takes the new investments of capital, or the number of workers, or the value of the total product, gold production always represents just 1 to 1½ per cent of the total production. The agricultural lands of Argentina attracted in 1910–12 five times more English capital than the whole of South Africa. A lack of capital [for commodity production] and an insufficient growth of production in all the other branches cannot therefore be a cause of the rise in prices of all commodities [according to Varga and Karski].

Karski goes even further. While for previous increases in gold production (in the eighteenth century and after 1850) he assumed a fall in the value of gold, he doubts that such a fall has taken place in the last decades, and therefore comes to the same practical conclusion as Varga. Theoretically he seeks to prove that improvements in gold production only caused poorer gold ores to be exploited, which means that not only the new capitals had to content themselves with the usual profit rate, but also that labour [power] and the costs per kilogramme of gold remained as they were. The mass of gold produced grew, but its value did not sink. The reason lies [according to Karski] in the fact 'that gold has a market price established by the standard of coinage [*Münzfuß*]', namely 2,790 marks per kilogramme. This is of course a baseless argument, because that figure does not represent the "price of gold" but expresses the *weight* of gold in coins of ten marks; the "price of gold" can only be expressed by the commodities that can be obtained in exchange for it, and if the prices of all the commodities that determine the costs of production of gold rise, the poorest gold ores cannot be profitably exploited. Kautsky has pointed out in his brochure that Varga's mistake

lies in the fact that he assumes what must be proved: the constancy of [commodity] prices. Because if [commodity] prices at some point rise, the poorer pits, which are supposed to keep gold prices up, will not be exploited.

In practical terms, Karski argues that things have not develop as favourably for the capitalists in the Transvaal mines after the Boer War as they hoped; the labour question remains unsolved, wages have increased, profits are not as high as they appear, only the founders' profits and the speculative profits are high. [According to Karski:] 'The fact that, as a consequence of a reduction in the costs per tonne of ore, in the Transvaal constantly poorer ores have been brought into exploitation, that in America and Australia an absolute decrease in the gold contents of the ores and deposits has been proved, while new rich gold fields and ores have not been discovered, has caused the average cost of production of gold to increase, and with it the value of money.' Although Karski is wrong in this general conclusion, we agree that precisely in the last years the production costs of gold in Transvaal have not only not decreased but increased considerably, above all because the richest ore deposits there have been gradually exhausted. But doubtlessly in the 1890s the production costs of gold had decreased significantly, and therefore the value of gold must also have fallen, which continues to have an effect on the current rise in prices. The question therefore remains: how does this event [a fall in the value of gold] lead to a general rise in prices?

This question was answered most clearly and completely by Kautsky in his recently-appeared brochure. If more and more capitals are attracted to gold production by a new technical procedure which reduces production costs and increases profits, it is not at all necessary, as Bauer thinks, for capital to be withdrawn from other, commodity-producing branches. The increased demand for machines, articles of consumption, etc. which the growing gold production brings about, drives up [commodity] prices, first of all in the gold land itself. That already prevents the poorest pits, which with constant [commodity] prices would be exploitable, from being exploited. In this general rise in the prices of the commodities needed for gold production is expressed precisely the fall in the value of gold, which makes the poorest pits unprofitable. If Varga were right, the gold mine owners would receive huge incomes as extra profits. Actually, the gold mines yield on average a significantly lower profit rate than the rest of the capitalist enterprises.

What with other commodities is brought about by the competition between producers [within the same production branch], who all want to sell and therefore depress prices, with gold happens through the growing demand for all the other commodities. All other commodities must first be sold, if the owner wants to buy something; an independent

demand therefore cannot develop; demand is only a consequence of the sale itself. Each [commodity] determines as it were the mass of the others; it is tied by strings to the entire economic body, and only moves when the whole body moves. By contrast the gold producers, to retain this image, wander about freely, and can pull forward the whole from outside, because their product, gold, appears as an independent demand for commodities, without being tied to any previous sale. If gold production increases, a growing mass of gold flows from the hands of its first owners, the workers and officials in the Transvaal, the share-owners in London, into the world, which appears as a free demand and therefore drives up prices. In this way is realised in practice the general rise in prices as a consequence of the fall in the value of gold. A lack of capitals for commodity production is not necessary [to explain the rise in prices]; the flow of capital into gold industry, as long as extra profits are to be made there, goes on and increases the demand for commodities until, through the rise in prices, profits have declined enough.

However, it seems not immediately clear how the relatively small gold production can exert such a powerful effect in the midst of the colossal world production. But this world production is a very elastic thing, very sensible to any force driving it forward or obstructing it. If the growing demand [due to increased gold production] causes a rise in prices in some branches, it stimulates [commodity] production in those branches, which in turn generates new demand for articles of consumption and machines and spreads the rise in prices to other branches or production. Otto Bauer has already emphasised this ever-wider expansion of the rise in prices once it has begun to develop. Gold production acts here as a stimulus for a favourable economic conjuncture, for a general prosperity, and the rise in prices through the fall in the value of gold appears as a moment in the regular cyclical fluctuation in prices. In the representation of this connection between gold production and the economic conjuncture lies above all the great significance and importance of Kautsky's exposition for our theory and our praxis.

But we will deal in detail with this matter elsewhere in this newspaper.[181]

[181][Pannekoek continued with a couple of other articles not included here (1913b, 1913c).]

Chapter Thirteen

The Measure of Value under Paper-Money Circulation (1922)

Wolf Motylev

Wolf Motylev (1899-1967) was a Russian economist. This postscript to his translation of Kautsky's 1912 article 'Gold, paper currency and commodities' was basically a restatement of Kautsky's thesis that paper money can replace gold as a means of circulation but not as a measure of value in the context of the early Soviet debates about monetary circulation under the NEP, which had been introduced the previous year. Motylev polemicised above all against Katzenelenbaum's endorsement of Hilferding's theory of 'socially necessary circulation value'.

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The question of the measure of value in a paper-money currency has caused and continued to cause disagreements not only among bourgeois economists, but also among Marxists. If however, in the pre-war time among Marxists the view predominated, and among bourgeois economists it was very widespread, that gold was the measure of value even under a pure [inconvertible] paper currency, the widespread adoption of paper money during the war and after it has raised doubts about the correctness of this view. In a significant number of countries [inconvertible] paper-money has almost completely displaced gold from the domain of circulation. Paper money, for all its deficiencies, has been already for a whole number of years the sole real and tangible money. The prices of commodities are expressed in paper money and this gives the impression that there is a [direct] link between commodities and paper money. The link between paper money and gold broke down and paper money for a long period already has apparently become independent of gold. All this creates the illusion that the real measure of value is paper money itself, without any reference to gold.

If, however, gold as a measure of value is rejected, and paper money itself is recognised as such, this necessarily raises the question of what determines the value of that measure of value – of paper money. It is obvious that, if we reject gold as a necessary measure of value, we have to look for an answer in the comparison of the amount of issued [paper] money with the aggregate value of the circulating commodities. Another way out of this difficult position would, obviously, be impossible. And, indeed, attempts have already been made to offer an

answer to that question along these lines. In the camp of Marxist youth, because of this, Hilferding's theory of 'socially necessary circulation value' enjoys success, because it provides an apparent answer as well as an appearance of harmony with the economic conceptions of Marxism. As regard bourgeois Russian scholars, every theory constructed by them, such as the 'conjuncture' theory of Tugan-Baranovsky[182] and the 'functional' theory of Nikol'skij,[183] asserts that the measure of value is paper money itself without any dependence on gold.

Let us look at such an attempt at a 'new' solution of the problem in a recent course on the theory of money by professor Z. S. Katzenelenbaum,[184] who substantiates his viewpoint by reference to the contemporary paper-money currency in Russia.

Indicating that for Marx paper money is a 'token of value' [Marx did not say that paper money was a token for value but a token for gold] and 'representative of gold', Katzenelenbaum writes:[185]

> It is easy to observe that this reasoning of Marx cannot explain the phenomenon of paper money in periods of its very sharp depreciation, like, for example, in the 1919-21 period of paper-money circulation in the USSR.[186] From that point of view, for example, it would be necessary to think that in 1919-21 paper money could circulate in Russia because it continued to serve as a "representative" of gold, and even more than this, that these tens and hundreds of billions of rubles, which figured in circulation at that time[187] "represented" a certain amount of gold. Taking into consideration that the population operating with paper money in Russia already by 1917-8 had almost forgotten how gold coins looked like, one can hardly regard those coins as the basis upon which the circulation of paper money was built at that time.[188]

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[182]Tugan-Baranovsky 1917. [In the phase of depression the general price level of commodities falls, exchange and the circulation of money slows down, credit is reduced, which leads to an increase of the value (understood as purchasing power) of money. The opposite occurs in the phase of expansion.]

[183]Nikol'skij 1892.

[184]Katzenelenbaum 1921, volume 1. [Based on courses delivered in 1916–19 at Moscow University. Zacharij Katzenelenbaum (1885–1961), was a member of the board of Gosbank (1921–29). A victim of Stalinist repression in 1930, his case was revised in 1933 and he was given a job in Magadan, then transferred to work (1933–38) in the Moscow finance department of Dalstroy, the organisation which ran the Kolyma gold mining camps. Katzenelenbaum proposed a psychological variation of the quantity theory of money (1925a, see Bortkiewicz's review 1927) and later wrote a book on South African gold industry (1954).]

[185][Our translation of this quote is based on the fourth edition of Katzenelenbaum's book. Motylev might have slightly paraphrased Katzenelenbaum's original. Just before this quote, Katzenelenbaum had cited a passage from *Capital* (Marx 1976, p. 225: '...If the quantity of paper money issued be double what it ought to be...').]

[186][Motylev quotes only: 'It is easy to observe the stretch in the reasoning of Marx'.]

[187]['these 55 billion rubles which figured in circulation on 1 January 1919' – number and date were given two pages earlier by Katzenelenbaum]

[188]Katzenelenbaum 1921, p. 138 [pp. 228–9 in fourth edition]. [Katzenelenbaum goes on: 'One can speak, and one must even speak about the historical continuity and historical link between the value of paper money and

Katzenelenbaum indicates that in Marx there is, however, another explanation of the nature of the value of paper money, far more acceptable.

> "Gold – says Marx in A contribution to the Critique of Political Economy – circulates because it has value, [whereas] paper money has value because it circulates". He pronounces himself even more determinedly about this issue later in Capital. Having put the question: "why gold is capable of being replaced by simple tokens that have no value", Marx arrives at the answer, that this is possible because the "functional existence" of money "absorbs, so to say, its material existence", and that within the sphere of internal circulation paper money is able "to receive a purely functional mode of existence in which it is externally separated from its metallic substance".[189]

Katzenelenbaum believes that the 'functional theory does not fit with the above given views about the "representative" [of gold] character of paper money'.[190]
Katzenelenbaum formulates and justifies the purely functional theory of [paper] money in the following way.

> Money [according to this theory] receives its value ... from the labour which it realises in the economy ... that is, it has not a *substantial*, but a *functional* value. Money is itself a useful commodity; useful, precisely, as money. At the same time, money is itself a commodity, limited in its amount ... The amount of paper money in circulation is limited because it can be issued only by determined institutions, empowered to do this by the state and in limited amounts. Usefulness and rarity – two qualities, which are quite enough for a thing to have value. From this also money gets its value ... The value of money arises in the sphere of money circulation, and not outside it.[191]

It is clear from the content of the above passages that between Katzenelenbaum's point of view and Hilferding's there are elements of similarity.[192] As Hilferding, Katzenelenbaum

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gold coins at a transitory period, at the early stage of the transformation of banknotes into paper money. But to consider this link permanent, performing its effect during the whole time of circulation of paper money is impossible'.]

[189]Katzenelenbaum 1921, p. 35 [p. 57 in fourth edition. The Marx quote given by K. on functional value (Marx 1976, pp. 226–7) is the same one used by Varga 1923.]

[190][Motylev gives no page reference here.]

[191]Katzenelenbaum 1921, p. 34. [p. 55 in fourth ed.]

[192][Katzenelenbaum (1922, p. 12) did note that Marx's criticism in *Capital* (1976, p. 220) of 'the absurd hypothesis that commodities enter into the process of circulation without a price, and money without a value', can be leveled at Hilferding. He claimed, however, that also Marx himself presupposed the application of the

considers redundant the 'detour' for the explanation of the value of [paper] money through gold; as Hilferding, Katzenelenbaum believes that the value of paper money is determined directly by the relation between the amount of [paper] money [in circulation] and the mass of commodities. Only that with Hilferding this is clothed in Marxist phraseology.

All this gives to Kautsky's article, the most detailed critic of Hilferding's theory of money, its burning and contemporary character.

Kautsky's critique, owing to its clear and solid analysis, proves to be directed against every attempt to determine the value of paper money independently of gold.

The fundamental error of all attempts lies in the confusion between value and price. The prices of commodities are the expression of their value in money. But it is clear that this expression presupposes not only a determined value of commodities, but also a determined value of money itself. Therefore paper money can only be a token for, a substitute, a representative of gold money. It enters the circulation process with a determined value – the value of the gold coins of the same denomination.

And only because of this can it measure the value of commodities.

Is the introduction possible under capitalism of new paper tokens, completely independent of gold, with arbitrary denomination? It is obvious that such a possibility is precluded by the very mechanism of the capitalist economy, which requires a money-commodity.

But even if we ignore this circumstance, such paper tokens would be impossible already because no commodity-owner would know how many tokens his commodity amounts to, and the government would have no criteria for determining the amount of tokens to be issued.

Indeed that socially-necessary minimum circulation, about which Hilferding speaks, cannot be calculated in labour-hours under capitalism. It is obvious that the government can determine the amount of tokens to be issued only by determining this 'minimum circulation' through some sort of gold currency or through a token equivalent to a certain amount of gold; only under this condition can the individual commodity-owner ascertain the value of his commodity. The circulation of paper tokens with arbitrary denominations and independently of gold is clearly a utopia. But this means that the theory of paper money circulation cannot abstract from the fact that paper money is a representative of gold, and that the purely functional theory of Katzenelenbaum as well as Hilferding's theory, which also abstracts from gold, in fact silently proceed from the golden value of the paper money entering into circulation.

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quantity theory in explaining the value of paper money.]

All this is brilliantly confirmed by the experiment made in order to introduce a new paper money in Lithuania in 1922. The government decided to issue it with the arbitrary denomination of 'lita'. Could it however do without establishing the gold value of the 'lita'? Obviously not. And indeed it was established that 10 'litas' are equivalent to one dollar.[193] Only a value of the 'litas' thus measured in gold gave the possibility of turning it into money, otherwise it could not even have entered into circulation.

Like Hilferding, Katzenelenbaum also believes that the historical origin of paper money in metal money has no meaning for the theory of the value of paper money. The fact of the emergence of paper money from gold does not prove, in their opinion, that the measure of value is gold and not paper money.

It is entirely indisputable, of course, that the actual, outwardly perceptible measure of value of commodities under a paper money currency is paper money. However, why can it perform this function? *Only because it was itself earlier measured in gold! Paper money, as measure of value, has, so to say, a golden nature. The measure of value is not paper money as a token, but paper money as a representative of gold.* Thus, the fact of its origin from metal money determines wholly the 'representativeness' of its nature! ...

The circumstance that by an excessive issue of paper money or by the changing factors of the conjuncture, the value of paper money can fall independently of real gold, and that, consequently, there is an immediate relationship between the value of the mass of commodities and the value of paper money, in no way refutes the above-mentioned viewpoint. Because for the changing correlation between the value of the mass of commodities and the amount of money [in circulation] to be reflected in the exchange rate [*kurs*] of paper money, *it is necessary, for it to be measured in gold and to have a 'golden value'. In this way, gold continues also in this case to be the measure of value; the essence of paper money, as a measure of value, is golden.* And the further paper currency proceeds in its course away from gold, the worse it is for it; the more negative is its influence on the national economy; the more likely is the possibility of its collapse.

Let us return now to Katzenelenbaum's reasoning. Did gold continue to be the measure of value in 1919? Without a doubt it continued to do so, because the circulation of paper money was itself measured in gold, and paper money continued to be the 'representative' of gold. Which gold? That which determined the value of paper money when it first entered into circulation, with which it circulated at any given moment, and from which it derives the ability to serves as a measure of value. [Under a paper money currency] gold is turned into an

[193][One dollar was equivalent to 1/20.67 ounce of gold. So 1 litas = 0,150462 gram of gold.]

ideal representation, but its real 'representative' is paper money. Regardless of whether the population remembers 'how gold coins look', paper money continues to be a 'representative' of gold.

What meaning however does Marx's exposition about the 'functional existence' of money have, and does it really not fit with the view about the 'representative' character of paper money? – Katzenelenbaum simply did not understand Marx! For the theory of money Marx characteristically distinguishes the individual functions of money and studies the nature of each function. With his exposition about the 'functional existence' of paper money Marx wants to emphasise that paper money arises from the function of money as means of circulation. 'Paper money', Marx says, 'has value because it circulates'. This means that paper money arises from money's function as means of circulation. But, Marx emphasises, it has an existence only '*externally* (our italics) separated from its metallic substance'. In reality, its existence is not independent of its metal substance and the function of measure of value continues to be performed by gold, the 'representative' of which it also is. In the thought of Marx gold 'can be substituted by simple tokens that have no value' wholly and fully only in the function of means of circulation. In the function of measure of value it is, therefore, entirely the *representative* of its measuring gold.

In this way, Marx's exposition only emphasises the independent 'functional existence' of paper money in the function of means of circulation, and its 'representative' character in the function of measure of value.

Let us now return to the examination, in light of Marx's theory of money, of one of the burning contemporary problems, the problem of creating a reliable measure of value, which has very direct relation to our subject. This question called forth, as is known, an animated and fruitful discussion on the pages of *Pravda*, *Ekonomicheskaya Zhizn* and *Torgovo-Promyshlennaya Gazeta* [*Newspaper of Trade and Industry*], as well as lively debates in circles of economists and statisticians. At the present moment this discussion can be considered basically finished. Wherein lies the essence of the problem? In the task of finding a stable (although relative) measure of value, which could enable us, under the unsteady oscillations of paper currency, to carry out the calculation of prices and, in general, all the practical estimations, as well as computations of general economic significance. As is well-known, the struggle took place between the advocates of a 'commodity' ruble and the advocates of a real gold ruble.

First of all it is necessary to note, that the very fact of posing the question about a reliable measure of value is a corroboration of Marx's theory of money. Because it proves that the

more the exchange rate [*kurs*] of the paper rubles falls in comparison to the gold coins of the same denomination, the more unstable is their gold value, the more weakly it manifests itself in them, and the less fit is paper money for carrying out the function of measure of value, because it represents gold to a lesser degree. It is no less important for the subject under discussion to note that the 'commodity' ruble represents, in substance, the pre-war gold ruble. The commodity index, which is the basis of the commodity ruble, is nothing else than a number indicating how much the present prices of a certain group of commodities have risen, in comparison to the prices of this same group of commodities before the war. But the pre-war prices of commodities are nothing but their value expressed in gold. Consequently, the commodity ruble ultimately derives the price of commodities expressed in contemporary paper money from the amount of pre-war gold they represented. All this confirms that paper money is a measure of value only as the representative of gold.

But supporters of the universal applicability of the 'commodity' ruble tolerate one error, which is reflected in their estimation of the scope of its applicability. They tacitly assume that the commodities have not changed in value compared to 1913. Only such an assumption allows them to equate contemporary prices to the pre-war prices. Meanwhile, it is clear that production costs, the value of commodities, have actually risen so much that present prices and pre-war prices, regardless of their accurate expression, are not at all equal. That is why, when calculating prices with commodity rubles at pre-war prices, one must be very careful and correct them with coefficients, using specific indexes for each given branch of industry. If we also take into account that indexes, as statistical magnitudes, must inevitably lag behind actual developments and moreover depend on the method of their calculation, it becomes clear that the 'commodity ruble' cannot have universal applicability as reliable measure of value. It can be used at best only as an indicative quantity; it is just a method in computation, s [statistical] calculation for a given period.

As for reliable measurement, then, the more suitable method for doing this is at present real gold. Of course it cannot yet be an absolutely reliable measure of value and it only very slowly will approach such ideal. But it already appears as a comparatively more stable measure of value. It is unlikely that the rise in the exchange rate of the gold ruble which took place in the autumn will be repeated to the same extent. Due to its significance as world money, to the facility of its transportation and storage, to its qualitative uniformity and so on, gold has an incontestable chance to acquire, earlier than other commodities, a uniform market quotation at an all-Russian scale. If we add to this, that the exchange rate of gold enables us to make reliable estimations for monetary policy, then the benefits of a real gold ruble

compared to a statistical commodity ruble becomes obvious.

The exchange rate of real gold is more suitable for the establishment of market prices and for commercial accounting, because it reflects changes in the market conjuncture and thus makes possible a quicker reaction to these changes.

All of this applies also to banknotes, as authorised representatives of real gold.

From this it does not follow, that we should forget that the most real option [for monetary policy] for the time being are nonetheless prices in paper rubles. As long as gold does not become a means of circulation, as long as it remains a commodity, the purchasing power of paper money in relation to commodities and its exchange rate in relation to gold cannot fully coincide. Therefore for some operations, demanding an exact and full depiction of actual market prices (calculation of cost price and so on), actual contemporary prices in paper money should be used.

Let us resume. Contemporary paper money continues for the reasons set out above to have a golden value. But precisely because of the fact that the golden value already appears weakly in paper money, the need emerges for additional and auxiliary 'rubles'. All this only confirms the correctness of Marx's theory of money.

Chapter Fourteen

'Hilferding or Marx? (A Contribution to the Critique of the Theory of Money of Hilferding)' (1926)

Vladimir Poznjakov[194]

In his work on *Money and credit* Finn-Enotaevsky writes:

> Money appeared at a certain stage of the development of *exchange* in kind, having become ordinary. Some of the functions fulfilled by money, which a series of prominent economists see as the essence of money, had a place in social economic life also *before* the appearance of money, and they will exist *after the disappearance* of money: let us indicate though the fundamental function of money, to serve as *measure* of value. It is only in the sphere of *commodity* circulation that a *particular* commodity, fulfilling the functions of *measure* of value and *means* of circulation together, becomes *money*.[195]

It is difficult to purposely press such big confusion in so little space, to the length altogether of a few lines. Firstly, what are these functions of money which existed before the appearance of money and will remain also *after* the disappearance of money? In any case these will be functions of something else, but not functions of money. Secondly, Finn-Enotaevsky calls the property of such functions their function to serve as *measure of value*. But a measure of value presupposes value, because one cannot measure that which does not exist. With the result that we, evidently, blissfully arrive at the view of, at least, also Adam Smith, who, for example, saw money as a means which people agreed to resort to for the sake of convenience.[196] Value, measured by money, exists, evidently, by itself, independently from money, yet the same money has under this not the slightest relation to value. If the first with proper interpretation is true, then the second already is absolutely untrue. The issue here is, of course, that value, at least in this place in Finn-Enotaevsky, clearly acts in the quality of a

[194][Economist, frequent contributor to *PZM*. Polemic on the place of gold in the schemes of reproduction with Tadeos Avdalbegjan (1885–1937) (see appendix Marx 2011).]
[195]Finn-Enotaevsky 1925, p. 29.
[196]'In order to avoid the inconveniency of such situations (that is in natural exchange of commodity for commodity. *V.P.*), every prudent man in every period of society, after the first establishment of the division of labour, must naturally have endeavoured to manage his affairs in such a manner as to have at all times by him, besides the peculiar produce of his own industry, a certain quantity of some one commodity or other, such as he imagined few people would be likely to refuse in exchange for the produce of their industry. Many different commodities, it is probable, were successively both thought of and employed for this purpose' (Smith 1909, pp. 29–30.).

logical category. Adam Smith saw money at the same time as a commodity. Likewise Finn-Enotaevsky considers it further also to be a commodity, and even a *particular commodity*. But this particularity lies only in, – as this follows from the latter, – the point that this commodity fulfils the 'functions of *measure* of value and *means of circulation'*. Finn-Enotaevsky perfectly manages to see the basic fault of a 'series of prominent economists' in that they derive the essence of money from this or the other function of money. But Finn-Enotaevsky's entire distinction from them lies in the point that, in his opinion, again expressed here, the essence of money is the sum of two of its functions. It is perfectly true that it is mistaken to deduce the nature of money from any one function of money, but undoubtedly too, it is no less mistaken to deduce money from two functions at the same time; in this case quantity does not yet change into quality.

That here Finn-Enotaevsky presents the situation quite incorrectly, he himself also knows, because further he says:

> The connection of paper money – and the bank-note – with the value of a sort of *exclusive* commodity, let us say, a precious metal – lies in the nature of money, and not merely practical convenience introduced due to the natural variability of credit as R.G. Hawtrey believes: it is ineradicable, as long as exchange exists, which created money. And money is a commodity, though also a particular one.[197]

Thereby comes before our sight the question about the nature of money. What answer do we find in Finn-Enotaevsky? 'This same process, – he says, – which turns the value of commodities into *prices*, turns the commodity, with which these prices are expressed, into *money*'.[198]

It is clear that the nature of money also should be derived from this process. But such formulation of the issue is at bottom false. However, our task does not at all lie in the critique of the views of Finn-Enotaevsky; the task, which we set ourselves, is different: it is to submit to an examination the basic errors of the theory of money of Hilferding. If we involved also the case of Finn-Enotaevsky, then only because he in the cited words in a very pure form gave in essence a very accurate formulation of the basic views of Hilferding, and therewith, let us add, repeated also all his errors.

Let us turn all the same to the characteristics of this process with which money arises. We just indicated that the presentation of this process by Finn-Enotaevsky we certainly cannot

[197]Finn-Enotaevsky 1925, p. 67.
[198]Finn-Enotaevsky 1925, p. 29.

recognise as correct, because it at bottom contradicts Marx's theory of money, which we see as the sole right one. But at the same time it is, in an unsurpassable manner, so to say, internally connected with his presentation about money, as measure of value plus means of circulation. Actually, but not in words, a similar presentation about the process, as Kautsky tried to show, lies in the kind of foundation on which Hilferding raises his whole theoretical construction (in the domain of the theory of money, of course). Incidentally, in relation to Hilferding, as we will see further on, also that is untrue.

Can we not, in fact, assert, that the process, which turns a particular commodity into money, is the process of the modification of values into prices, like this is claimed by Finn-Enotaevsky? We think, that this cannot be done under any case. However, by the way, the natural consequence of such an understanding is his presentation that there is a place for value while at the same time money still is non-existent and, oppositely, – value could exist, even if money would be obliterated, like this is claimed by the same Finn-Enotaevsky.

Marx gave a quite different answer; for him the process of turning a particular commodity into money was at the same time the *process of development of value itself*, and not merely a conversion process of values into prices. This moment in a strange way falls out of the sight not only of Finn-Enotaevsky, but also of Hilferding, and likewise also of the critics of the theory of money of Hilferding. However to the theory of Marx we return later, as for now let's turn to our nearest theme.

As is known, Hilferding constructs a new concept of 'socially necessary circulation value',[199] and lays with it the basis of his theory of paper money; so he puts the question, at least, in *Finance capital*, but, as Kautsky shows,[200] later on, he spreads the by him derived position also to the case of gold currency.[201]

The examination of his basic errors is made therefore actual; all the more since also 'among the camp of Marxist youth, – as comrade Motylev asserts,[202] because of this (that is due to the transition of almost all countries to paper money currency. *V.P.*) the theory of 'socially necessary circulation value' of Hilferding enjoys success, giving a manifest answer and, – moreover, – an appearance of harmony with the economic conception of Marxism'.

With a special critique Kautsky exposed this new theory of money in his article *Gold, paper and commodities*.[203] But it must be said, that the basic flaw in the Hilferdingian construction

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[199]We intend to translate *Wert* with the term 'value' [*tsennost*]. The term value [*stojmost*] we will use only in citations, where it is used in the source. [Note by V. Poznjakov.]
[200]Kautsky 1912.
[201]Hilferding 1912a.
[202]Motylev 1922, p. 164.
[203]Kautsky 1912.

remained for Kautsky unnoticed; therefore his critique to a great extent misses the mark. Furthermore Kautsky himself gets mixed up later, trying to restore the by Hilferding broken (of course, only in the presentation of Hilferding himself) connection of paper money to gold. Comrade Motlyev sharply, but still not sharply enough, shows the incompatibility of the views of Hilferding and the theory of Marx. Unfortunately, this incompatibility he does not show closer.

However let us turn to the original work: we need first of all to set forth the by us criticised theory. Luckily for us, the notoriety of Hilferding's views relieves us of the necessity of their detailed exposition. Let us stand still at the key points of his theory and give them moreover in a certain critical perspective.

Here in him the methodological approach itself is curious already. Kautsky quite correctly characterises it, saying that 'money, according to Hilferding's formula, must function first as a measure of value and then still have functioned as a means of circulation, before its value becomes determined, which makes of it a measure of value and a means of circulation'.[204] It is only a surprise that Hilferding, having written so much and well about Marx's method, in this concrete case so thoroughly forgot all his writings, and not in the smallest degree could apply this method. Here he absorbed well the language and style of Marx, but the substance or method of Marx remained for him terra incognita.

Concretely, in reality we meet, of course, firstly with money in its various functions. No exchange, that is circulation of commodities, no money also, – exchange precedes money. But in the acts of exchange money functions in the form of means of circulation, because the aim of the act of exchange also is the transference of the commodity from hand to hand, effectuated by means of money. Likewise, only in exchange we meet money functioning in the role of measure of value, because measuring the value in order to exchange it (sell or buy). One can say the same also concerning the other functions. Only with the fulfilment of these functions, a distinct commodity becomes money. These functions, apparently, also were historically forerunners; from them, apparently, also must begin the analysis of money: from these functions of money must be derived its nature. And we know that all kind of bourgeois theories of money present at once such an outline of the nature of money from this or the other of its functions. One can even try to derive the essence of money from all of its functions, understanding this in the sense of a simple, arithmetic sum of these functions. And, still, even also in such case this would be an incorrect path. Because the whole in this case will be more, than a simple sum of its parts. Concretely we are given various functions of

[204]Kautsky 1912, p. .

money. But 'the concrete is concrete because it is the *concentration [a synthesis]* of many determinations, thus a *unity in the diverse*',[205] but not unity of the diverse. 'In thinking, it therefore appears as a process of concentration [summing-up], as a result, not as the starting point, although *it is the real starting point*, and thus also the *starting point* of perception and conception'.[206] Therefore there is no greater mistake than the path on which Hilferding arose. But it predestined likewise also his basic error, because actually we have in him a barely consistent, only covered with Marxist phraseology, variant of the vulgar quantity theory. However, at this moment of methodological order we will have to stand still later in connection with the theory of money of Marx, which we will have to touch, in order to show, to what extent Hilferding substantially 'revisioned' Marx.

On the necessity of such revision of the views of Marx, incidentally, Hilferding also himself speaks. In his opinion, we encounter a series of such phenomena, – as, for example, the phenomena of the monetary system in the Netherlands, Austria and India, – which we with the help of the formulation of Marx's theory, have apparently been incapable of solving.[207] The theory of money developed by Hilferding, as he himself says or as it seems to him, on the basis of Marx's theory, must solve precisely these advanced new phenomena of monetary currency problems. That under this he comes to correct Marx – this is indisputable. The whole question also lies in the point, what character does this correction carry? And is not such 'repair' soon a distortion of Marx?

Hilferding begins his analysis with setting up 'the necessity of money'. Here (in the first chapter of his *Finance capital*) he deals only with gold money, and here he, seemingly, only recounts that which was said by Marx. But this is only in appearance; because with attentive reading it becomes clear, that the theory of Marx is subjected not to distortion , - this cannot be said frankly, but it is sort of embellished, taking on inappropriate proportions, as if a reflection in a curved mirror. That which is the more essential, which characterises the theory of money of Marx, sort of slips away, the other way around, it is disproportionally inflated in other relations, receiving with this the form of a trampoline, which helps Hilferding to accomplish the leap to his actual theory (the issue here, in reality, is not about a 'correction' to Marx's theory, we add in parenthesis, but precisely a jump *from* Marx's theory). Even where Hilferding just merely follows Marx, expounding fully Marxist, on the surface, views, we have already a thorough revision or highly significant deviation from the

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[205]Marx 1986a, p. 38. [Modified translation.]

[206]Ibid. [Modified translation.] (italics in citation mine). Marx says further: 'The method of advancing from the abstract to the concrete is simply the way in which thinking assimilates the concrete and reproduces it as a mental concrete. This is, however, by no means the process by which the concrete itself originates'.

[207]Hilferding 1981, preface p. 22.

views of Marx, with which, of course, Hilferding *volens nolens* in these cases proceeds, alas, to repeat only the tail of pronouncements made not only long before him, but also before Marx.

Now the question in general stands thus: or the theory of Marx, in full, without any corrections; or these corrections and little adjustments, and the inevitable repetition of the new wisdom of bourgeois political economy – *tertium non datur*. So, what is money?

> Money is a commodity like all other commodities and thus embodies value.[208]
> As a value money is like any other commodity, and the necessity for it to have value arises directly out of the nature of the commodity producing society.[209]

This is entirely true, so true, that later, when Hilferding goes on to build his theory, he entirely forgets about these definitions. Hilferding knows that money in general is a commodity, that, as such, it must have and does have value, he knows also, that money at the same time is a particular commodity. Because 'it is differentiated from all other commodities by being the equivalent of all of them and thus expressing their value. It acquires that status as a result of the *whole process of exchange*'.[210]

We, in this way, arrive at the process of exchange, that is to the phenomenon of commodity circulation. This commodity circulation, precisely *circulation*, as the 'whole process of exchange', also is for Hilferding the starting point. Incidentally, on this he himself says:

> Historically, money originated in circulation and is therefore *primarily a medium of circulation* (for Hilferding money also *theoretically* is firstly a medium of circulation. *V.P.*). Only after it has become a general measure of value and the general equivalent of commodities, does it become a general means of payment.[211]

With these words Hilferding accentuates his theory against Knapp, but he accentuates it not only against Knapp!

And fully in accord with this he says, that 'the necessity for a common measure of value – in which the value of every other commodity is directly expressed, and with which every commodity can consequently be directly exchanged – arises *from the process of exchange, from the need continually to equate commodities with each other*',[212] that is, from the series

[208]Hilferding 1981, p. 33. (chapter 1)
[209]Ibid.
[210]Ibid. Italics mine.
[211]Hilferding 1981, p. 378.
[212]Hilferding 1981, p. 33. Italics mine.

of acts of exchange, in other words, from the process of exchange as such.

> Money is, therefore, on the one hand a commodity, but on the other hand it is always forced into the unique position of acting as a general equivalent for all the others.[213]

And he more closely characterises this process of being forced. 'This has happened through the action of all other commodities, which have legitimated it as their sole and universal equivalent'.[214] Money, for Hilferding, is legitimated in the quality of general equivalent commodity.

But further on this commodity itself in him disappears, because the centre of gravity he brings precisely to this legitimation. Only because of this legitimation it becomes money, the direct embodiment of socially necessary time. But in this Hilferding entirely forgets that extremely significant circumstance, which Marx purposely stresses, that such directly-social labour turns out to be private labour, precisely the labour producing gold. In this Marx sees one, and moreover an extremely significant for the theory of money, contradictory form of value. This side of the question is completely erased by Hilferding, and instead of this he puts in first place precisely the process of circulation or the act of exchange. In general the first chapter of *Finance capital* could have perhaps been considered not a wholly successful presentation of the theory of Marx, if not further on a very clear light was thrown on this peculiarity in its presentation, – otherwise Hilferding could not all have moved to 'socially-necessary circulation value'. In this concept also is included the whole sense and at the same time the whole nonsense of this theory, if it is approached with a critique on the basis of Marx's method.

If this absurd red thread runs already, although in an encrypted form, through the whole first chapter, – the reader easily can trace it himself,[215] – then in open and unmasked form it officially comes onto the scene later (in the second chapter). True, his theory, – at least in *Finance capital*, – Hilferding builds for a paper-money currency, however it strikes a further goal; theoretical construction in general has its logic (as the Germans say: he who says A, must also say B), and it with equal success or, more accurately, with the same failure must be expanded also to a [restricted] metallic, specifically gold money currency. Incidentally, in his later article[216] Hilferding also gives it such a broadened interpretation.

So, let us reveal the content of the concept 'socially-necessary circulation value'; for this let

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[213]Ibid.
[214]Ibid.
[215]I point out at least pp. 22–3 of *Finance capital*.
[216]Hilferding 1912a.

us give the words of Hilferding himself:

> The circulation process takes the form: Commodity–Money–Commodity, or C–M–C, –Hilferding says (we will see later what use he makes from this formula and what interpretation he gives it). – In this process, money furnishes *simply the evidence* that the individual conditions of production for any single commodity coincide with the general conditions of social production.[217]

This is true, *if* we stay within *only* this process; however at the same time, logically, for us money will already be given before this process. Because, as this is pointed out by Hilferding himself, 'money provides circulation *in the first phase* with a value-crystal into which a commodity can be converted, only to be subsequently dissolved into the equivalent value of another commodity'.[218] But in Hilferding not only money is dissolved into the equivalent commodity form, at the same time in him also the theory of value and the theory of money of Marx is dissolved into something resembling the vulgar position of bourgeois quantity theorists. In fact, directly after this he continues:

> But it (money. *V.P.*) is indispensable as a value-crystal [*Wertkristall*] because it is a necessary means of giving *society's sanction* to the value of a commodity [*weil nur so der Wert der Ware gesellschaftlich gültig ausgedrückt wird*]. Thanks to money, it is possible for value to be reconverted from its monetary form into *any other* commodity.[219]

With this 'society's sanction' we encounter already the specific Hilferdingian deviation; further on he develops it in the following way:

> The monetary expression of value is only ephemeral, and unimportant *in itself* ... what is important for our purpose is *exclusively the social aspect* of money – its quality of

[217]Hilferding 1981, p. 37. Italics mine.
[218]Hilferding 1981, p. 38. (chapter 2)
[219]Ibid. Earlier in relation to gold money Hilferding said: 'The producer does not learn... until after the completion of the exchange... that he is a fully-fledged member of a commodity producing society... The only proof he has of his usefulness as a member of society is another article ('The object which is authorised by the common action of commodities to express the value of all other commodities is – *money*', – Hilferding says a little below) which he obtains in exchange for his own. The thing which can give the producer this assurance must therefore have the necessary authorization (from the side of society. *V.P.*)'. Hilferding 1981, p. 32. Here he still speaks about a *thing*, but further on, as we see, he belies all connection with this *thing*, that is, with the particular *commodity – money*.

> being the value [*stojmost*] equivalent of a commodity.[220]

Let the reader not think, that this 'value [*stojmost*]' is the value of money itself, that is, that material from which money is made. This 'value' is separated from this despicable commodity body with which it earlier was connected, and gets a particular abstract, non-material existence. For, though 'this social aspect of money finds its palpable expression in the *substance* used as money, for example, gold', 'it can also be expressed directly through *conscious social regulation* or, since the state is the conscious organ of commodity producing society, by state regulation'.[221]

Firstly, good that there is this 'conscious social regulation' in a principally non-organised, non-regulated society! Secondly, regardless of the sharp dissociation of Hilferding from the state theory of money, here are highly noticeable traces of influence of the Knapp-ist position; and, thirdly, this 'conscious social regulation' Hilferding connects with a determined material, and if, as in the given case, he connects it with gold, then this is not at all necessary, but a purely incidental connection. Gold in the given case can be substituted by paper; because the value of paper is not the value of the paper material itself, *but a reflection of the value of the commodity opposing money*. Here we came *in medias res* of the theory of Hilferding; in *Finance capital* he develops his theory with application precisely to paper-money currency, but, as we have pointed out, there is no logical obstacle to broaden it also to the case of any money currency.

However let us give the formulation of Hilferding himself:

> Under a system of pure legal-tender paper currency,[222] given a constant velocity of circulation, the value of paper money is determined by the total price of all the commodities in circulation. The value of paper money in such circumstances is *completely independent of the value of gold and reflects directly the value of commodities*, in accordance with the law that its total amount represents value equal to the sum of commodity prices divided by the number of monetary units of equal denomination in circulation. It is obvious that paper money can appreciate as well as depreciate in relation to its original value.[223]
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> Thus, – Hilferding sums up, – the value of paper money is determined by the value of

[220]Hilferding 1981, p. 38. Italics mine.
[221]Ibid.
[222]We already pointed out, that if in general the correctness is recognised of the views of Hilferding, then this position must be spread also to metal money currency.
[223]Hilferding 1981, p. 39. Italics mine.

> the total quantity of commodities in circulation. The proof that value is a purely social category is supplied by the fact that a mere slip of paper, worthless in itself, discharges the social task of circulating commodities, thereby *acquiring a value which is out of all proportion to its negligible value as paper*, entirely worthless, *but the value of the mass of commodities, - presenting the reflected value of commodities onto paper signs*. Just as the moon, long since extinguished, is able to shine only because it receives light from the blazing sun, so paper has a value only because commodities are impregnated with value by social labour. It is therefore a reflection of labour value which converts paper into money just as it is reflected sunlight which enables the moon to shine. The luster of *commodity value* is to paper currency what the rays of the sun are to moonlight.[224]
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> The magnitude of the value of this 'measure of value' itself (paper money and metallic under suspended coinage) is no longer determined by the value of the constituent commodity, gold, or silver, or paper. Instead, its 'value' is really determined by the total value of commodities in circulation, assuming the velocity of circulation to be constant. The real measure of value is not money. On the contrary, the 'exchange rate [*Kurs*]' of money is determined by what I would call the *socially necessary value in circulation*.[225]

One does not have to demonstrate that this kind of theoretical construction badly tallies with the basics of Marx's theory; incidentally this is seen also by Hilferding himself. Marx wrote:

> Worthless tokens become tokens of value only when they represent gold within the process of circulation, and they can represent it only to the amount of gold which would circulate as coin, an amount which depends on the value of gold if the exchange value of the commodities and the velocity of their metamorphoses are given.[226]

These words of Marx also Hilferding gives, but he *only* does not agree with the, in his opinion, detour, to which Marx resorts. 'The detour by which Marx proceeds – first determining the value of the quantity of coins and then, from that, the value of the paper money – seems superfluous'.[227]

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[224]Hilferding 1981, p. 40. Italics mine.
[225]Hilferding 1981, p. 47.
[226]Marx 1987, pp. 352–3.
[227]See Hilferding 1981, p. 383, footnote 32. And he continues: 'The purely social character of that determination is far more clearly expressed when the value of paper money is derived directly from the social value in circulation. The fact that, historically, paper currency had its origin in metal currency is not a reason for

The whole question also lies in how correct such a direct deducement is? Is it an accident, in fact, that Marx 'became entangled' on a detour? Does there not lie a necessity for such a detour in the nature itself of commodity society? Does not Hilferding himself say, that 'labour time (included in the commodity. *V.P.*), as such, does not get direct expression', that for this is demanded comparison to another thing, that is an amount of this 'other thing', and such a 'thing', as the same Hilferding clarifies, which itself possesses value. And further - in polemic against the quantity theory of money - did not Hilferding himself say:

> Finally, it is impossible to compare between a mass of bullion on one side and a mass of commodities on the other. What relation is supposed to exist between *n* kilograms of gold or silver, or even paper, and *a* million boots, *b* million cases of shoe polish, *c* bushels of wheat, *d* hectoliters of beer, etc.? A reciprocal relation between money and commodities presupposes that they have something in common; in other words; it presupposes the value relation, which is precisely what has to be explained.[228]

But it is even more absurd to compare an amount of commodities on one side and a bundle of paper money on the other, and to this also leads the whole 'new' breakthrough of Hilferding. After all 'the token of value is directly only a *token of price*, that is a *token of gold*, and only indirectly a token of the value of the commodity',[229] and with that precisely a symbol of the value of gold, and not of any other commodities, nor of the whole mass of commodities. This is what Marx affirmed, and something else he could not affirm. It is very good, that Hilferding gives here the entirely correct position of Marx, it is very unfortunate only, than he now already also forgets about it; however, we will return yet to this question. The theory of value of Marx also logically is tied in with it, the logically from it following theory of money is absolutely irreconcilable with Hilferding's own theory and with his 'socially necessary value in circulation'.

The starting point of Hilferding serves, as we saw, Marx's formula of commodity circulation C–M–C; together with it, money for him acted firstly and exclusively, as the mediating link in this formula of commodity metamorphosis, that is as means of circulation; true, it at the same time fulfils a certain social function, it gave social recognition to the labour of private commodity producers, it acted as measure of value; but this function of being the measure of

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regarding it in this way theoretically. The value of paper money must be deducible without reference to metallic money'.

[228]Hilferding 1981, p. 47.

[229]Marx 1987, p. 350. These words Hilferding cites (1981, pp. 58–9).

value is subjugated by Hilferding to its fundamental function as means of circulation, stems from it. Hence, Hilferding deduces the nature of money from its functions, and precisely from the function of means of circulation; this deduction lies clearly or covertly at the basis of any quantity theory. The absurdity of such a deduction of the nature of money from the formula C–M–C jumps every Marxist in the eyes; therefore Hilferding carries out this same operation, but in a more complex form; he starts not from two individuals, but the chained together metamorphosis, he takes all commodity circulation of the given society.

> Let us assume, – he says, – that, at a given time, circulation requires 5,000,000 marks for which 3,600 pounds of gold would be needed. We should then have a total circulation as follows; 5,000,000 marks in C –5,000,000 marks in M –5,000,000 marks in C. If paper tokens were substituted for gold, their sum would have to represent the total value of commodities (5,000,000 marks in this case) whatever their nominal value. In other words, if 5,000 equal notes were printed, each note would be worth 1,000 marks; if 100,000 were printed, each would be worth 50 marks. If the velocity of circulation remained constant and the sum of prices were to double without any corresponding change in the quantity of paper money, the value of the paper would rise to 10,000,000 marks; per contra, if the sum of prices were to decline by one half, the value of the paper would fall to 2,500,000 marks.[230]

Wherein lies the fundamental error of the entire construction of Hilferding? Although his *Finance capital* sometimes also was called the fourth volume of *Capital*, however this theory of money, of course, could not receive unanimous recognition among Marxists. The fundamental error of his theory his critics see in the confusion between value and price. 'The fundamental error, – Motylev says, – of all similar attempts lies in the confusion between value and price'.[231]

Kautsky in his critique of Hilferding[232] unwinds it in two directions. 'He *equates value and price*'[233] – Kautsky says. 'The way from value to price is precisely the detour that Marx adopted... Hilferding spares himself that "superfluous" detour by regarding price and value as *identical concepts*'.[234] And further:

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[230]Hilferding 1981, p. 39.
[231]Motylev 1922, p. 166.
[232]Kautsky 1912.
[233]Kautsky 1912, p. .
[234]Ibid.

> Value is determined by the socially necessary labour time. If a socially necessary labour time of 5 million hours of work goes into the production of a given mass of commodities, its value will be accordingly high. If an hour of labour produces 1/1395 pounds of gold, and if one calls that amount of gold a mark, one can also say that the sum of value of the mass of commodities amounts to 5 million marks. Strictly speaking, however, this is not a sum of values but of prices, that is, a determined quantity of values expressed by a certain amount of gold, against which it is exchanged. Value and price are by no means the same thing, although to simplify matters one can sometimes equate one with the other. But therewith one must not forget, that the expression of the value of a commodity in money presupposes the value of the latter, and that it is senseless without this presupposition. It is always more accurate, to call such an expression price.
>
> Why does then Hilferding talk about a sum of values rather than a sum of prices? The sum of value of commodities is given; it is independent from the value of gold. The sum of prices, by contrast, presupposes not only a certain value of commodities, but also a certain value of gold. Equating the sum of values to the sum of prices enables Hilferding to make the price as well as the value of commodities independent from the presupposition of a given value of money.[235]

So, the fundamental error of Hilferding, in the opinion of Kautsky, and, incidentally, also of other Marxists, lies in the fact that he confuses or identifies value and price. But this objection, firstly, is not true, and, secondly, even if it were true, it is not complete, moreover it itself suffers some vagueness and allows various interpretations, one of which could be correct, in another interpretation the objection itself falls under the same objection which can be made at the address of Hilferding.

It is untrue because Hilferding definitely distinguishes such concepts as value and price.

Given the quantity of commodities, – he says, – changes in the quantity of money in circulation follow the fluctuations of commodity prices, regardless of whether such price changes arise from real changes in value or only from fluctuations of market prices.[236]

And these words are found precisely in the second chapter, where he, as we know, develops his specific theory of money. Kautsky thinks that Hilferding simply compares the sum of prices of commodities, on the one side, and the whole mass of circulating paper money, on the other. But price is the monetary expression of value in money, and precisely in money,

[235]Kautsky 1912, pp. 148-9.
[236]Hilferding 1981, p. 37.

possessing its own value; this expression in 'real' (that is in gold) money Hilferding also drops from view. However it is a necessary condition and necessary prerequisite for some reasonable comparison of the commodity mass on the one side and paper money on the other. After all paper money possesses no value of its own and, therefore, cannot be the material which expresses the price of commodities; the price in this case is presupposed, as given, and it is the given expression of the value of the commodity in gold. All this, of course is true, but this in no way affects the construction of Hilferding, because, in his opinion, – and this is the centre of gravity of the question – paper money *possesses* its own value; it is – not the value of the monetary material, it is – not even the value of the by it represented gold, it is – a functionality, a reflection, an objectivisation of the value of the mass of commodities. And in as much as this is so, – we avoid, firstly, confusion of value and price, and, secondly, we get rightly speaking also the monetary (in *such* money) expression of value.

The socially-necessary labour time, residing in some commodity, compares with a certain amount of the whole social labour time, reflected and objectivised in this wad of paper notes. Here is fully admitted also the change of value in price, and therewith also the oscillation of price. Another question is, to what extent is such objectivisation permissible?

We pointed above also to the incompleteness and certain vagueness of these objections; Kautsky, for instance, says; 'What do we have according to Hilferding's presuppositions? A *mass of values*, a heap of commodities'.[237] Two pages further he says again: 'In contrast, in Hilferding's formula we have, as already remarked, *the sum of values of commodities*, which must be transformed into their sum of prices even before the value of money is determined'.[238]

These passages can, perhaps, be understood thus: if we cannot in the wake of Hilferding speak about the sum of prices, because for this is required the presence of gold (even if also in contemplated presentation), then, in reality, we can speak here about the sum of values. But would we be right to do this? Here we also turn to that formula of Hilferding, about which Kautsky reminds, and which we already brought up earlier, and at the same time get the second objection of Kautsky against Hilferding.

This formula, as we know, has the following form: C–M–C, with which is represented in Hilferding the *whole* of commodity circulation of this society. Kautsky precisely in such interpretation of this formula sees the 'peril' for the entire Hilferdingian construction; in this he is undoubtedly right; but this peril he sees not at all there, where it really happens, and together with this his argumentation misses the mark.

[237]Kautsky 1912, p. .
[238]Kautsky 1912, p. .

> C–M–C is, – Kautsky says, – the formula for the circulation of *individual* commodities. What Hilferding wants to represent by it, however, is not the circulation of particular commodities but the circulation of the entire mass of gold and commodities in society. But that is the result of numerous circulation processes, which are intertwined in the most diverse ways, and which cannot be collectively represented by the formula C–M–C. In that formula, the value of C must be always equal to M. In contrast, the total value of the money in circulation is almost never equal to the total value of the commodities in circulation.[239]

Here Hilferding, in the words of Kautsky, drops out of view such a simple moment like the velocity of the circulation of money. And Kautsky imagines that together with this falls also the entire theory of Hilferding! But this is not at all an objection: it takes only a distraction from this velocity of circulating money, to assume, for instance, that all acts of exchange happen *simultaneously*, - and theoretically this is fully sufficient, because in the opposite case one would have to throw out also the teaching of Marx on reproduction, – in this case, we maintain, if something falls, then it is precisely the objection of Kautsky himself. 'In that formula (C–M–C), *the value* of C must be always equal to M', he says. Well, do we have in general here this right to speak about value? In this lies also the whole question; in this lies the fundamental fault of the theory of Hilferding, here lies also the difference between Marx and Hilferding. Let us give again the already cited words of Kautsky: 'In contrast, in Hilferding's formula we have ... the sum of values of commodities, which must be transformed into their sum of prices'. We maintain, on the contrary, that in Hilferding's formula we have not anything, that it represents by itself a tautology, that there is no content in it at all. There is not only no price in it, but also no value.

In fact, Kautsky himself notes, that it is obtained through the summation of all acts of exchange, committed in the given society. But the whole does not always equal the sum of the parts: sometimes the whole has a little more, than simply their sum, sometimes, – here we also have such a case, – the sum of the parts can give absolutely not any whole. The quantity changes in the complete absence of any quality, and hence, also of quantity (incidentally, also this has, however, a certain qualitative change). Although this absence of quality already had a place also in every individual formula, but only in covert state, and did not jump so much in the eyes.

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[239]Kautsky 1912, p. .

As is known, this formula in Marx represents the chaining metamorphosis of two individual commodities. In it two commodity-owners meet face to face, possessing these two commodities. Its objective meaning is in the exchange of one use-value C1 – for the other, distinguished from it, use-value – C2 for the first commodity-owner, and the exchange of C2 for C1 – for the second. We ignore the third person – the possessor of money, in this connection he interests us not.

Let there now be in front of us a series of commodity-owners A1, A2, A3, A4 .... B1, B2, B3, B4 .... , let us denote respectively the commodity of everyone – C'1, C'2, C'3, C'4, ... – C''1, C''2, C''3, C''4 .... Let them further enter into deals of exchange, accomplished in pairs between A1 and B1, A2 and B2 and so on, and let us assume, that they all together constitute the whole commodity circulation in society.

So, for the category-A sellers the matter will take such form:

C'1	–M–	C''1
C'2	–M–	C''2
C'3	–M–	C''3
C'4	–M–	C''4
	....	
	....	

But circulation will take such a form, if we will look on this commodity dance from the point of view of the commodity-owner A1, A2 ... But every sale for one is a purchase for another. From the point of view of B1, B2, B3, B4 .... this commodity dance will look differently:

C''1	–M–	C'1
C''2	–M–	C'2
C''3	–M–	C'3
C''4	–M–	C'4
	....	
	....	

The sum of these two tables also gives us the *whole commodity circulation* of the given society. We get, hence, the following detailed formula:

C'1+C'2+C'3+C'4+	**{–M–}**	C''1+C''2+C''3+C''4+...
..C''1+ C''2+ C''3+C''4+....		...C'1+C'2+C'3+C'4+...

In the left part we have the sum of all sold commodities, in the right – the sum of all bought commodities; but both here and there – these are the very same mass of commodities. Every commodity figures first among the sold commodities, but as every sale for one is at the same

time a purchase from the point of view of the other contractant, then this same commodity hereafter emerges among the crowd of sold commodities. Or differently this could be put as such: a certain determined mass of commodities in a certain moment is *simultaneously* brought to the market. In order that every individual commodity-owner accomplishes C' C'', it is necessary, that his C firstly exchanges with M; for all the C, in this way, is accomplished C–M, the whole mass of commodities is replaced with money, all commodities on the market are sold. Then it would be necessary to begin the second act – M must exchange with C. But this M–C already occurred. Because every C–M was at the same time also M–C. We here ignored the third person – the possessors of money, because they in this case cannot help us; in the extreme situation we would have had only to involve here the previous metamorphosis. And now let us put here in place of M the Hilferdingian paper money, this immediate reflection of value of the circulating mass of commodities, and we arrive at this very simple result that in front of our eyes not only money possessing its own value disperses in equivalent form, but that thus also value itself disperses, the theory of value of Marx is left somewhere on the side *sine usu*, and together with it Hilferding's own theory disperses in the typical absurdity of the quantity theory. Speaking plainly, before us in classical, law-like form is a *reductio ad absurdum*.

One and the same mass of commodities, lying right and left from the wad of notes, reflects, for Hilferding, in this wad of notes its value; in other words, this mass of commodities expresses its value in the reflection of its own value, that is it under these conditions becomes a certain unknown economic thing-in-itself.

The reader, probably, noticed already, that we arrived at the simple, accidental or single form of value:

> C – M
> or
> commodity A is worth *y* commodity B.[240]

The entire singularity of the Hilferdingian theory lies, in this way, in the point that it slips here in place of Marx's M a wad of notes and then nonetheless claims, that it has before itself the form of value. In fact his formula, does not express any form of value, coming down, at most, to the self-affirmed existence of a certain mass of use-values.

As every Marxist competent reader easily realises, the error of Hilferding lies in the point

[240]Marx 1976, p. 139.

that time like 'labour time, as such is not expressed directly ... it is expressed only in the exchange commensurability of two articles',[241] here he forgets about this fundamental position and wants to express it directly, having captured its reflection in a scrap of paper, presented to a given bundle of commodities. It is not appropriate, hence, to see this error in a confusion between value and price; in him both these economic categories disappear in an equal extent; at the same time his 'socially-necessary circulation value' takes on the form of a mysterious phoenix, his paper money – this immediate reflection of commodity value – becomes a reflection of an unexpressed and in such counter-position by no ways expressible value, that is a reflection of that which does not reflect and in general here cannot be reflected.

The inevitable consequence of this is a fatal vicious circle, in which Hilderding lands. This curious idem per idem consists of the following. Like we already remarked, Hilferding distinguishes between value and price. But the value of money is directly reflected in 'socially-necessary circulation value', or, in the final light, the value of the mass of commodities, divided by the velocity of circulating money. However the value of paper money he determines as, – and cannot define otherwise, – the sum of prices of commodities.[242] If he also speaks sometimes of values, then, when all is said, he inevitably moves down to prices. But what is, for Hilferding, the price of a commodity? It is its value, expressed with money, by the quantity of the value of money transforming and its quantity. But the value of money is a reflecting objectification in money of the sum of prices of commodities, which in its turn depends on the quantity of the value of money. Thus, the value of money determines the price of commodities, but the price of commodities depends on the value of money. Incidentally, if we for a minute agree with Hilferding, that money reflects the *value* of commodities, then also in this case we do not escape from this vicious circle; it changes only the flatness in which it will rest.

Otherwise it also could not be, once in the foundation of the whole theory lies a tautology, not containing in itself an expression of values, nor an expression of prices. As is not strange, the theory of Hilferding still long before its appearance was submitted to special critique from the side of Marx.

> In the circuit C-M-C, – he says, – *in so far as* it (that is the token of value. *V.P.*) expresses merely the dynamic unity of the two metamorphoses or the direct transformation of one metamorphosis into the other – and this is how it appears in

[241]Hilferding 1981, p. 31.
[242]Hilferding 1981, p. 38.

> the sphere of circulation, within which the token of value operates – the exchange value of commodities assumes in the price merely a nominal existence and in money merely an imaginary or symbolic existence. Exchange value thus appears to be something purely conceptual or an imagined entity but possessing no reality except in the commodities, in so far as a definite amount of labour-time is materialised in them. *The token of value* (Hilferdingian money. *V.P.*) *therefore seems to represent the value of commodities directly*, since it appears to be not a token of gold *but a token of the exchange value which exists solely in the commodity and is merely expressed in the price. But the appearance is deceptive.* The token of value is directly only a token of price, that is a token of gold, and only indirectly a token of the value of the commodity.[243]

With these words Marx, in this way, already anticipates the future 'breakthrough' of Hilferding and very categorically marched out against similar interpretations and 'deepening' of his theory.

The path, on which Hilferding arrived at such an amazing result, we characterised above. Money for him is before all else a means of circulation, and this function, and likewise in connection with it and playing a perhaps subordinate role, its function as measure of value, put in place the foundation: proceeding from them, Hilferding tries to get to the nature of money; but he goes, when all is said, there, where he also cannot avoid going once the path is selected: to the very superficial, vulgar theory of money, and to the renunciation of the basis of the economic theory of Marx.

We tried to follow after him on the path of his reasoning and in conclusion arrived at the simple, single or accidental form of value. And this is no accident. Because the starting point of the Marxist theory of money at once also is this simple elementary form; from this Marx deduces the nature of such a phenomenon as money.

> The difficulty in forming a concept of the money form, – Marx says, – consists in clearly comprehending the universal equivalent form, and as a necessary corollary, the general form of value, form C. The latter is deducible from form B, the expanded form of value, the essential component element of which, we saw, is form A, 20 yards of linen = 1 coat or *x* commodity A = *y* commodity B. *The simple commodity form is therefore the germ of the money form.*[244]

[243]Marx 1987, p. 350.
[244]Marx 1976, p. 163.

'The whole mystery of the form of value lies hidden in this elementary form'.[245] At the same time 'the riddle presented by money is but the riddle presented by commodities; only it has become visible and blinds the eyes with its metallic shine'.[246] And this is completely understandable, because the simple form of value includes in itself also the whole content of the theory of commodity fetishism. What does this simple equation or, better said, equality mean? It shows, that for the expression of the value of any commodity the availability is *necessary* of, at least, two commodities. One – which expresses exchange value, and the other in which this value is expressed, but expresses it with its own material body. Commodity A, standing in the left part of the equality, located in the relative form of value, this is primarily some use-value, but in the given expression figures from the point of view of its owner only as exchange value, then as the equivalent form (or commodity B in the equivalent form) is primarily exchange value itself, but not exchange value by itself, - it here not at all gets any expression, - but the exchange value of commodity A, reflected in the use-value or body of commodity B; hence, in this expression it is primarily and merely use-value, and simultaneously the expression of its own opposite – value, yet the exchange value of commodity A. In other words, value, – and we know, that it is a determined social relation, – exists as some quantity of a thing (commodity B). And the whole difficulty of the disclosure of both commodity fetishist society in general, and of the riddle of money fetishism, and, therefore, also of the nature of money, consists precisely in understanding this simple form of value. At the same time this side of the question completely escaped from the recognition of bourgeois economy – even classical.

> Now, however, we have to perform a task, – Marx says, – never even been attempted by bourgeois economy. That is, we have to show the origin of this money-form, we have to trace the *development of the expression of value* contained in the value-relation of commodities from its simplest, almost imperceptible outline to the dazzling money-form. When this has been done the mystery [riddle] of money will *immediately [at the same time]* disappear.[247]

So, we now can respond to the question: what is money? Money is a commodity, but a commodity, having become the universal equivalent: with the commodity-equivalent simple

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[245]Marx 1976, p. 139.
[246]Marx 1976, p. 187. ['Metallic shine' is in Struve's Russian translation 1907.]
[247]Marx 1976, p. 139. [In Struve's translation: '...*development of value*, as expression of the exchange relation of commodities...']

form of value we have, in this way, already money *in potentia*. The subsequent development from the simple or accidental form of value to the money form, will be simultaneously a *process of development of value itself*, just only proves, how the equivalent form for all commodities coalescences with a particular commodity, which also becomes money in facto. And the main principal difficulty lies not here, not in this development of the equivalent, but precisely in the very emergence of the equivalent, in the simple form of value.

True, the value of this commodity-equivalent itself in this form of value gets not any expression; but it *necessarily is assumed*, because otherwise there will not be also the form of value itself. Here also lies the difference between the theory of money of Marx and the theory of money of Hilferding. Because the latter allows the possibility of the expression of value of one commodity (the whole aggregate mass of commodities of this society in this case becomes one commodity) in things, not possessing any value. But this, as Marx shows, would mean the direct expression of social labour time residing in commodities, and therefore assumes a socially-regulated process of production. But such organisation of society has no place at all for money.

However the definition of money as a commodity, having become general equivalent, still is a little abstract; it is devoid of concrete content, though it already is included in it. Strictly speaking 'so far, however, we are acquainted with only one function of money, namely, to serve as the form of appearance of the value of commodities, that is as the material in which the magnitudes of their values are socially expressed'.[248] This is the exceptionally important function, which characterises the qualitative determination of money. But it is at the same time, as we only just showed, also exceptionally abstract, because here there is still not a quantitative determination money, that only also gives the concrete determination of money. Classical political economy studied only the latter question, whereas it did not at all form an idea about the existence of the other side of the question. About the existence of this qualitative side Hilferding knows, but in his construction it actually is blurred, and *eo ipso*, regardless from his subjective aspirations, he slides to the position of bourgeois economy.

Money – this special commodity – expresses the exchange value of all other commodities; but it expresses with this not only their value in general; it expresses the *determined* by its quantity exchange value. From this the second function of money: - money, as measure of value. But weightless weights cannot measure; as measure of value money must therefore possess its own value. Moreover, eliminating this internal value of money, we also eliminate the very form of value, and, therefore, also value. But the expression of the quantity of value

[248]Marx 1976, p. 184.

requires also a determined unit of measure; by its nature it carries thereto a completely contingent character. Here, and only here, we meet with the role of state, this 'conscious organ of commodity producing society'.[249] Here, and only here, also one can speak about conscious 'legitimation'.

But the commodity owner, this individually acting agent on the market, follows such a 'roundabout' expression of the value of his product not for his enjoyment. This process is at once the market process, the act of exchange. Its goal – to move the commodity from the hand of the commodity producer, for whom it is not a use-value, into the hands of his contractant. This exchange act is at the same time only one link of social commodity circulation; money together with this emerges in a new quality, as the mediator in this act, it gets a new function – the function of means of circulation.

We need to stand a little more at money in the function of means of circulation, though because, from this function of it Hilferding also deduces its essence, as direct reflection of 'socially-necessary circulation value'. As Marx already notes, the very process of money circulation leads to the separation of the monetary denomination from its actual content. Because money (gold) under circulation deteriorates; its nominal value already ceases to coincide with its immanent value; therewith money becomes a token of value. But a token of value, born in the process of circulation, also can function only in the quality of means of circulation, in the quality of middle term of C–M–C.

But we already saw, that this formula C–M–C, as symbol of all commodity circulation of a given society, boils down in essence to the simple form of value, to the form

C – M.

But also for every individual act of exchange this form of value (C–M), though also not visibly stepping forth, all the same is a presupposition. Commodities in circulation step forth as determined values, but this also means, that every given commodity already took its place in this formula, that it, located in the relative form of value, already has expressed its exchange value in the opposed to it equivalent – in money. But a token of value such an equivalent cannot be. Hence, a token of *value*, for instance, paper money, separated from its real expression of the value of the commodity in the commodity-equivalent, possessing therefore its own value, *ceases to be even a token of value*, because here there is no value at all, it becomes simply a scrap of degraded printed paper. *Such* paper money ceases to be also money.

The conception of paper money, in as much as we speak about it, as about money,

[249]Hilferding 1981.

necessarily therefore *includes* in itself the conception of such a general equivalent, which has real internal value, the token of which it also is. Signs of value are, therefore, signs of gold, as money par excellence. But it is not at all obligatory, that this gold therewith actually enters in circulation.

In fact, let us turn to that formula, which we got at the conclusion of our critique of the theory of Hilferding.

C – Δ (in the form of some bundle of paper money).

We showed, that here, strictly speaking, there is not even the form of value. It gets this meaning only in the case if we will regard this heap of paper money as representing some amount of gold, that is if we put under it a gold foundation:

C – Δ (heap of paper)

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M (gold)

The laws, from this relation, we can formulate briefly, resorting, after Hilferding, to the optical metaphor. He, as we know, regarded money as direct reflection of those rays of value, which proceed from the general commodity heap. But the entire point is that these rays are invisible, and in conditions of commodity production they *directly* cannot be detected by any means. They can only be visible in the case when they are expressed in another thing, in money, and only *if this thing itself possesses an equal level of value*, but which at the same time, nonetheless, here does not get any expression. These value rays by a 'detour' reflection also reflect onto paper money. The force of this reflection, as is clear from the first view, hinges on two moments: 1) on the force of the value of the original light, that is M (on the amount of gold) and 2) on this square, onto which it diffuses, or in which it is reflected, that is on the amount of circulating tokens of value.

In its turn, the quantity of M determines the quantity of C; but it is not at all obligatorily equal to it. For every given moment, in every individual metamorphosis of C – M both C and M must be equal quantities in value. But for the series of successive moments this interrelation disappears, because one and the same M can successively *n* times reflect the value of commodities. But what is more important, - the real amount of this M (gold) not at all is necessary; real it must step forth only if for now it should be a factual transition of commodity from hand to hand, but with this money remains only a means of circulation, but, as such, it can be also a sign of value. But, since for circulation really existing money is demanded, even though really existing signs of value, then simultaneously this raises the question also about the necessary amount of it. Determining this amount, Marx also deduces

his formula, the determined amount demanded for circulation of money, here, and only here, also emerges socially necessary value in circulation.

We leave aside the other functions of money; for our goals enough also was said, because now must be completely clear the essence of the theory of Hilferding, as well as the whole difference between Marx and Hilferding. Hilferding's straight path brought him very far of the side from Marx: money for him again turns in a sort of riddle, in a sort of mystical thing. In conclusion he appears helpless before a series of phenomena of real money currency; but the 'detour' path of Marx gives us a strong Ariadne thread and leads us out of the most complex problem of this real money currency. For illustration we also stop in conclusion at one prying example.

Kautsky in the above named article characterises the theory of Hilferding, as a genuinely Austrian theory.[250] In fact, the phenomenon of money currency of Austria, and such analogue facts, relating to the Indian rupee, undoubtedly gave a direct push to Hilferding to revise the Marxist theory of money. In Austria and in India he meets with an extremely prying phenomenon: after both these countries, under the existence of silver currency, had transitioned to a restricted system, and the free coinage of gulden and rupee was discontinued, their course rose above parity. The value of metal coin – gulden and rupee – already no longer were determined by the value of silver. 'Monetary theorists are still plagued', – Hilferding says on this case, – 'by the question: What constitutes the measure of value when coinage is restricted? Obviously it is not silver (nor gold, if gold coinage would be restricted)'.[251] However also Kautsky, critical of Hilferding, exactly this circumstance also put in some difficulty. From this difficulty he tries to get out in the following manner: he asks the question under which conditions this happened? – Under the existence of gold valuta and gold circulation in all other countries. Thereby, in Kautsky's opinion, gold factually is the measure of value also in Austria and in India, regardless of their silver currency. Under silver gulden and silver rupee he slips in this way gold, circulating in the quality of money for all other, at least, developed capitalist countries. But what in the case with a restricted gold currency? What then is the measure of value? For theoretically the case of such restricted gold currency is entirely thinkable. The theory of Marx gives us on this question a very simple answer. Incidentally, this answer also Kautsky himself gives, in his later work: 'The value of paper money does not get determined by the labour which is really put in it, but it is determined by the socially-necessary labour, namely the labour, which would be socially necessary to bring forth that amount of gold (which we from now on regard as the only

[250]Kautsky 1912, p. .
[251]Hilferding 1981, pp. 46–7.

money metal), which in the process of circulation is replaced by paper money'.[252]

If the value of paper money here Kautsky boils down to the value of gold, which would circulate if there was no paper money, then the value of the silver gulden and rupee and even of restricted gold coin would be determined on the basis of the exact same principle. For they with the suspension of free coinage turn essentially into simple signs of value, or in paper money, but printed on gold or silver [that is, a token coin]. And for the explanation of similar kind of phenomena there is not any necessity to undertake a revision of Marx and construct a 'socially-necessary circulation value', which does not explain anything, and furthermore contradicts in the most categorical way the basics of the theory of value of Marx.

[252]Kautsky 1918, p. .

Chapter Fifteen

Gold, Money, Paper. A Rebuttal to the Theory of Money of Varga (1923)

Eduard Ludwig[253]

I. Gold and commodities

1.

The form under which the currency problem appears, is the deviation of the paper mark from the gold mark, which shows itself therein, that a paper 20 mark note is worth only still a small fraction of a golden 20 mark coin, that an American dollar, measured in German paper mark, is worth a multiple of 4.20 mark.[254] The cause and scale of the devaluation of paper money, compared with gold money, is to be explained.

This question is answered in principle, once it is understood, why in the first place a worthless piece of paper with the stamp of the state of 20 marks can be equated in circulation with a valuable golden 20 mark coin, just as in fact this equation has for decades taken place in Germany. The deviation is to be derived from the equation. In other words: the paper money crisis must be developed exactly as a moment in the process of money circulation, like the economic crisis as a moment in the capitalist total process. It is therefore also not a hole in the Marxist system, when it does not occupy itself at length and widely with the problem of the disagio and the variability of the exchange rate of currency. But rather the solution to this problem, the possibility and the unavoidability of an under valuableness of paper money, as measured by the homonymous gold coin, in certain phases of development of capitalism, is contained within the by Marx developed laws, by which money can be *completely* replaced by value tokens. It is just a matter of deploying these laws of 'normal' money circulation to the phenomena of the abnormal currency deviations. Only in this way can at all the new sort of currency problems in the breakdown of high capitalist Germany become a touchstone of the Marxian money theory, like the latter conversely in its actual probation gives the proletariat, for whom the overcoming of the monetary disaster has long become a practical political task, a means for the fulfilment of this task.

Comrade Varga, in his article 'On the problem of the currency stabilisation',[255] heads the opposite way and comes thus consequently not to an application of the Marxist monetary theory to the money depreciation, to an explanation of the phenomena from the laws of

[253][Eduard Ludwig Alexander (1881–1945), an important economic theorist of the KPD.]

[254][The prewar exchange rate. By June 1923 one dollar surpassed 50000 mark. This article presumably appeared in late June.]

[255][Varga 1923, not translated here because Ludwig quotes it abundantly.]

Marxism, but to a repealing of the foundation of Marxist economy in general: the *law of value* in its application to the money circulation. In his concern, that he might be accused of the mechanical application of Marxism on the not yet completely collected facts of currency crisis, he gives, overwhelmed by the plethora of abnormal phenomena, the theoretical standpoint of Marxism up also for the explanation of normal money circulation.

2.

How can a paper slip become a symbol, a valid replacement of a gold coin? This core question of the whole currency problem Varga answered not, as Marx, by demonstrating that the 'full-valued' paper money receives its gold glimmer from the value of gold that it replaces in circulation, so that the value of the gold is the basis and indispensable presupposition for its replacement by value tokens in circulation. Rather he fashions the equality between the worthless gold ersatz and gold, the parity of the gold token with the gold coin, the 20 mark note with the 20 mark coin, by undressing gold of its own value for highly developed capitalism with central banks. In fact: if the gold with 20 mark coins is itself worthless, if it thus itself becomes value token, instead of remaining value, then its equation with a paper gold symbol encounters no more conceptual difficulties. Of course one obstructs oneself with this Vargaian paper money theory, which equates in principal gold and paper as worthless, instantly the understanding for the possibility of a deviation of paper money value from the gold money value, thus for the actual currency problem.
Varga says:

> This becoming independent of the price of gold from the production costs of gold gave the monetary unit an enduring stability and thereby facilitated the replacement of gold by means of circulation and payment without own value. The further capitalism developed itself, the more money *lost* its character *as a commodity with own value* (emphasised by me *E.L.*), the easier and smoother the replacement went of gold by in their natural form worthless money notes [*wertlose Geldzeichen*].[256]

From what reasons in advanced capitalism paper has increasingly displaced gold in circulation, will be considered later in another context. Important here is solely the sentence in which Varga takes from money its character as commodity with own value. It can admittedly in this formulation, whose understanding is complicated by the imprecise

[256]Varga 1923 p. 146.

expression of Varga featuring through the entire article, be still doubtful, whether 'the money', that lost its 'character as a commodity with own value', still is the gold money or already the always 'smoother' paper money replacing it. That however Varga with the money without own value actually means gold money, reveals the following passage of his article:

> The modern currency and central bank system has made the value of gold practically independent of the *present* production costs. The central banks of capitalist countries before the war have bought every amount of newly produced gold at a fixed price, that is they gave a fixed quantity of coined gold or equivalent banknotes for each offered amount of newly produced bullion. This meant that the gold producers for their products received an in advance fixed price. *Hereby the newly produced gold is eliminated from the group of those commodities whose value changes with a change of the labour time contained in them*.[257]

For a commodity whose value is not determined by the socially necessary labour time expended for its production, the law of value is repealed. Such a commodity is for Varga gold. Although it is – this cannot dispute Varga – a product of human labour; it is in its function as measure of value the materialisation of universal labour time,[258] that is, the labour contained in it becomes measure of value of all other commodities: but its own value is, in the opinion of Varga, not determined by the for its manufacture socially necessary labour time.

3.

How does Varga substantiate this strange result?

Once by adjoining to the commodity gold other commodities as fellow sufferers: cereals, in general all products, in whose price (like also with gold) a *ground rent* is included. He says:

> Gold becomes in a manner similar to the agricultural products a commodity whose sale price is not determined by the for production socially necessary labour time, also not by the production costs of those produced under the worst conditions quantum that for the supply of the market still is necessary, like with cereals …'.[259]

The error is obvious. Did Varga just yet speak of the *value* of gold, that should not change with the labour time contained in it, he speaks now suddenly of *sale price* of gold and cereals.

[257]Varga 1923, p. 145. Emphasis by Varga.
[258]Marx 1987, p. 304.
[259]Varga 1923, pp. 145–6.

The *production price* of a commodity – this Varga surely means, when he inaccurately speaks of its sale price – is now in *all* commodities, not only with those which realise a ground rent, different from their *value*. It is made up of the *cost price* of the commodities (advanced constant and variable capital) plus the *average rate of profit*. The entire Marxist teaching of the average profit builds itself up on this difference of commodity-values from their production prices. But neither to Marx nor to anyone else, who does not believe in the legendary contradiction between the first and third volume of *Capital*, it therefore occurred to say that the value of the commodities, that yields the production prices different from this value, is not determined by the for their manufacture expended socially necessary labour time. On the contrary: production price and ground rent in their deviation from commodity-values can only be explained on the basis of the law of value. The price of production is the form of appearance of value:

> It is always in the form of the market price, and moreover in the form of the governing market price or the market price of production, that the nature of commodity value presents itself, its character being determined not by the labour-time needed by a certain individual producer to produce a certain quantity of a commodity, or a certain number of individual commodities, but by the socially necessary labour-time; by the labour-time required under the given average conditions of social production to produce the total socially required quantity of the species of commodity available on the market.[260]

By the circumstance that there is a rent in the price of gold or cereals, since a part of these agricultural or mining products were produced under more favourable conditions, than corresponds with the production price, nothing is amended of the determination of the value of also these products by the law of value. Ground rent and production price are rather than a cancellation, a confirmation of the law of value, its enforcement on the market in the distribution of surplus value among the various agents of production of the capitalist economy. Varga's first reason proves the opposite of what it was supposed to prove: the validity of the law of value also for the commodity gold, the determination of its value through the for its production expended socially necessary labour time.

4.

There remains the second reason, which should demonstrate the repeal of the commodity

[260]Marx 1981, pp. 779–80.

character of gold. It is just as threadbare as the first. According to Varga, the value (or is it the sale price?) of gold decouples from the labour time required for its reproduction, yes, from its production costs, especially through the 'officially fixed purchasing price of gold':

> Since the central banks in fact bought up each amount of offered gold at the fixed purchasing price, so not the production costs – neither the socially necessary, as with the unlimitedly reproducable commodities, nor the production costs of under the worst conditions produced commodities group, like with cereals – regulated the price, *but rather the fixed purchasing price decides whether a gold mine can be operated or not*.[261]

But who decides on the fixed purchasing price of this odd commodity without value and 'regardless' of the cost of production? The governor of the Bank of England, the president of the German Reichsbank, the director of the Bank of France, the buyers of all gold? As powerful as these gentlemen may be: the abolition of the basic laws of the capitalist economy by fixation of a purchasing price for a commodity without value goes beyond their strength. Let us see, what is going on with the fixed purchasing price.

The owner of a pound of gold brings it to the Reichsbank and receives therefor 1395 marks in gold or in gold redeemable notes. This price of 1395 gold marks for a pound of gold is so fixed, so immutable, that it even is laid down in the German Coinage Act. Thus Varga is right?

No. Because if the gold producer melts the 1395 freshly coined gold marks – 69.75 20 mark coins –, then he has a pound of fine gold: exactly as much gold, as he had before. From the standpoint of the gold producer a completely senseless operation, precisely as senseless as when a linen manufacturer gives 100 yards of linen in one piece, to receive them back into 100 parts of each one yard.

Of this relation between gold bullion and minted gold would also then not be changed anything, if in the execution of a devaluation – for example in realisation of Parvus's plans[262] – on a coin of gold of the content of a 20 mark coin instead of 20 mark 2000 mark would stamped. The gold seller would then instead of 1395 gold marks now receive 139500 gold marks. The name of the coin would have been changed. The old fixed price of gold would, in coins expressed, be replaced by a new fixed price. But at the end of the arduous reminting the gold producer would again only have exchanged one pound of gold in coin form for a pound

[261]Varga 1923, p. 146. Underscored by Varga.
[262][For example Parvus 1921, p. 23.]

of gold in bullion form. The result would merely be that the long history of coin debasement would be enriched with a new chapter.

It is clear that *this* fixed purchasing price, which converts gold from its bullion form into the coin form, cannot decide whether a gold mine can be operated with profit or not. If the gold producer during operation of his mining would be guided solely by the officially fixed purchasing price: the production costs, which according to Varga do not regulate the 'price' of gold, would by themselves lead him to go hopelessly bust.

Let us follow the gold producer, who has changed his bullion into gold coins [before the war] and is rejoiced over the bag of ringing 20 mark coins, on his way. After his walk to friendly [Reichsbank president] Mr Havenstein, who indiscriminately accepted the gold at the legal price, starts for him first the walk to the examination, to the market, on which for him, as a capitalist production agent, it must be proved whether he has satisfied the conditions of capitalist production in the operation of his gold mine: whether he in his gold mine has drawn up the production costs and the ground rent. The gold mine entrepreneur whose *particular* production process generates gold, that is the *general* exchange commodity, is at the end of his production process in the possession of M, that is of the commodity in the form in which the capital can begin its circle M–C–M1 again. He need not anymore, to obtain capital in the form of money, change his commodities in the market back into money. But this advantage, of being relieved of the metamorphosis of C1 into M1 or at most of being able to be confined to the exchange of commodities into coin gold, is only apparent. It does not take from the produced gold its commodity character. Also the produced gold must contain, just like the linen of the linen manufacturer, value and surplus value, the M1 must as a result of gold production be greater than the in this production invested M, if the gold mine entrepreneur is to be able to continue production on at least the same scale and to realise both the average rate of profit and rent. His 1395 gold marks, the officially fixed price for the pound of gold, must thus enable him on the market to replace the for the generation of this pound consumed raw materials, the worn machinery, to cover the wage for his workers and leave over to him finally the average rate of profit and the ground rent. Are raw materials, machinery and wages for a pound of gold so expensive, that the average rate of profit is not achieved or ceases, then the gold producer must close up shop.

Things are therefore just the opposite, as Varga represents them. Not the production price of gold becomes by the fixed purchasing price an irrelevant, for gold production indifferent appearance, but rather production price of gold (including rent) determines gold production and directs the point of the fixed purchasing price, which it alone has: to be a *standard of*

division for the gold pound, a part of weight of it, the *standard of price*.

But is the production price of gold for gold production determined just as for all other commodities – otherwise with the 'unlimited demand' for gold at 'fixed purchasing price' the frequent bankruptcy of gold mining companies would not be comprehensible – then for the determination of the production price of gold holds also exactly the same as for the other commodities. The production costs can only be cut, the profit and ground rent raised by increasing the productivity of labour in the gold mines, which manifests itself therein, exactly as with all other commodities, that the gold producer *under reduction of the value* for a given amount of produced gold at the end of production process has more money in hand than heretofore, before he increased and intensified productivity. With gold production this process is only mystified because the product of labour itself already is gold, money material, which has a fixed price only therefore, that its coin name, as form of expression of this price, is a part of weight of the gold pound.

As now however the production price for the whole world of commodities can only be explained on the basis of the law of value, as it for all commodities of the world depends on the expended socially necessary labour time, the same holds for gold. Precisely then when the gold producer, who arrives so easily at money, proceeds to replace the consumed raw material and machines with the gold of the previous production period and to train with it new workers, the process of capitalist circulation M–C–M1 must also for him be proved. This capitalist circulation process, which the gold producer cannot break through, is however only explicable on the basic of the law of value.

Also here the examination of the Vargaian argument leads to the opposite of his result: to the confirmation, that gold, like any other commodity, is determined in its value by the socially necessary labour time contained in it, that is, that its value changes with a change of the necessary labour time.

5.

The misunderstanding of Varga is that he, precisely like he confuses value and purchasing price, also mixes up gold in its function as measure of value and as standard of price. Although he speaks of this for the grasp of Marxist monetary theory important distinction, it remains however in him without theoretical consequence.

As *measure of value* gold is commodity, must be *commodity*, that is, variable in its value like any other commodities. Shall C-–M be the exchange of equal values, then on *both* sides, the commodity as well the money side, the value must be objectively determined by the *same*

social conditions. This condition is on the commodity side the for the generation of the commodity expended human labour, measured by the socially necessary labour time. The commodity value is, because determined by social and therefore changing factors, not a once and for all fixed, invariable magnitude. It changes with the social production conditions, that constantly change the necessary labour time. Therefore, on the other side of the equation, if the value of commodities should be measured by M, M will become measure of values, M will be determined in its magnitude by the same, changing social factors. Otherwise an equation between C–M is not possible at all. Even gold as M, money, as equivalent of C, must therefore, if the law of value is not to flounder from the start, be determined in its value by the for its production expended socially necessary labour. Gold thus becomes measure of values only because it is a commodity.

Money becomes changed from measure of value into *standard of price*, by the fact that a pound of gold is divided in determined parts of weight. If the commodities measure their value in gold, attain a price, it is sufficient that gold as money itself is a product of human labour, has value, so that C–M can be equated. But for a certain amount of a commodity to be really exchanged with a certain amount of gold as money, this particular amount of money itself again must be measured. So that one pound of coffee can be equated e.g. with a 20 mark coin, the price of coffee expressed in 20 mark gold, the minted 20 mark coin, as expression of the price of one pound of coffee, must itself stand in a stable relation to gold as measure of value. The ratio of the 20 mark coin to the gold pound must be fixed, set. The value of gold, assessed in the for its generation expended socially necessary labour time, presents itself in a certain weight of gold: one pound gold is the product of a given labour time and becomes therewith measure of the value of all other commodities, whose production had cost just as much necessary labour time. The 20 mark coin becomes the standard of price, the pound of coffee can express its value in it, since it is a fixed part of weight, the 69.75th part of a pound of gold, and both, coffee like gold, are commodities, products of labour.

As measure of value money is thus variable in value, because commodity. As standard of price it is fixed, because it is a determined part of a certain weight of gold. It does not matter how great the value of a pound of gold and hence the value of the gold mark is: the gold mark is and remains the 1395th part of a gold pound and can only therefore be standard of price.

> As measure of value, and as standard of price, money performs two quite distinct functions. It is the measure of value as the social incarnation of human labour; it is the standard of price as a quantity of metal with a fixed weight. As the measure of value it

> serves to convert the values of all the manifold commodities into prices, into imaginary quantities of gold; as the standard of price it measures those quantities of gold. The measure of values measures commodities considered as values; the standard of price measures, on the contrary, quantities of gold by a unit quantity of gold, not the value of one quantity of gold by the weight of another. For the standard of price, a certain weight of gold must be fixed as the unit of measurement. In this case, as in all cases where quantities of the same denomination are to be measured, the stability of the measurement is of decisive importance. Hence the less the unit of measurement (here a quantity of gold)is subject to variation, the better the standard of price fulfils its office. But can gold serve as a measure of value only because it is itself a product of labour, and therefore potentially variable in value.[263]

Varga's fixed gold price thus turns out to be, if it is to have a meaning at all, the *standard of price*. This is admittedly different from the function of money as measure of value, which has as its basis gold as commodity, however can only be derived from it.
It helps Varga also nothing that he confined his theory of gold as a commodity missing own value to the *newly produced* gold, as he has already attempted this in his essay *Gold production and the rise of prices* (1911). Precisely this newly produced gold is produced *in a capitalist way*. And it cannot be fathomed after the above delineated, why the laws of capitalism would be repealed for this capitalist gold industry. On the contrary. If the value of gold, like all other commodities, is determined by labour time, then the value of all existing, also non-capitalist generated gold directs itself after the value of the capitalist produced, provided that the production conditions of capitalist gold industry have become the norm for the socially necessary labour time for gold production. To what extent the value of gold hereby actually is changed, is the object of statistical investigations. But these statistical studies must stay barren from the start, when they are undertaken out from the point of the worthlessness of gold or invariability of its value.

6.

The representation of Varga of gold as a commodity with dwindling value character and fixed price is a contradiction in terms. Land and soil is not a commodity, because not a product of labour. It has however a price, the capitalised rent, because as object of labour it yields a return in excess of the price of production, the rent. Gold is, also for Varga, a product of

[263]Marx 1976, p. 192.

labour, but would have no value, nevertheless a price. How this price without value comes about, remains as obscure, as it remains nebulous in what way a thing without value character can serve as general equivalent in exchange process C–M.

In some way the value of money serving as means of exchange must be measured: otherwise the law of value breaks. If the value of gold as money is not measured in terms of labour time, then another measure of value must be found. This sees even *Hilferding* (1912. Against it Kautsky 1912), who, supporting Varga already in 1912, like him denies the own value of gold circulating as money, when he – admittedly by surrendering the Vargaian theory of a fixed gold price – extends his paper money theory of the 'social circulation value' to the gold circulation.

Hilferding, through this by himself drawn consequence of his paper money theory, shows thereby not only the senselessness of his own Marx improvement, but refuted simultaneously also Varga's conception.

To determine the value of the supposedly worthless gold money in circulation, Hilferding gave for the value of the circulating gold money the following formula:

> 'Value of the total money = (total value of commodities) / (velocity of circulation of money), plus the sum of payments falling due, minus payments which cancel each other out, minus the number of turnovers in which the same piece of money functions alternatively as a means of circulation and as a means of payment' (Hilferding 1912).

This formula – derived from the Marxist one for determination of the quantity of circulating money and as such still to be explained – lets the value of the circulating gold money, under suspension of the own value of gold material, only still appear as a *reflex* of the sum of the values of the to be circulated commodities. But how the commodity values can be aggregated without first measuring themselves to a common third one, that itself must be a commodity and have value, wherewith it can measure, this remains Hilferding's secret, just as much as it remains Varga's secret, in what way gold arrives at a fixed price, can become standard of price, before it would be measure of value. According to Hilferding gold as money must circulate, so that it gets value. The opposite is true. Gold as money circulates because it has value, is a commodity. To establish this crucial point of his monetary theory against the bourgeois economists, especially against the quantity theorists, who derive the value of money and the price of commodities from the amount of means of circulation, Marx expended the greatest discernment in *A contribution* and in *Capital*.

Hilferding and also Varga, when they deny of gold as money the character of a commodity

with its own value, are basically quantity theorists. Although Varga in his cited essay of 1911 took the field against the quantity theory and still even in his recent economic quarterly overview of the *Internationale Pressekorrespondenz* regards the quantity theory – admittedly in my view with insufficient reasons – for paper money as refuted, because in spite of the with the *Cuno's* mark support action associated excessive new issuance of paper mark the prices have not risen: in spite of all that he comes to the consequences of the quantity theorists. In *Capital* it says about this:

> The illusion that it is ... prices which are determined by the quantity of the circulating medium, and that the latter for its part depends on the amount of monetary material which happens to be present in a country, had its roots in the absurd hypothesis adopted by the original representatives of this view that commodities enter into the process of circulation without a price, and money enters without a value, and that, once they have entered circulation, an aliquot part of the medley of commodities is exchanged for an aliquot part of the heap of precious metals.[264]

The 'absurd hypothesis' that money circulates without value, is the starting point of the monetary theory of Varga. His attempt to go beyond Marx, has led him to the side of those who Marx in that quote characterises more closely.
The refutation of the by Varga practised criticism of the Marxist teaching, that gold is commodity, thus must have value, so that it can function as money, has led to the confirmation of the Marxist conception for the 'normal' capitalism. There remains, to develop from this doctrine the paper money theory and the explanation of currency fluctuations.
This will be done in a second essay.

II. Gold money, paper money

> These notes, when used in lieu of gold and pearls,
> are handy, too; you know right off how much you own
> and can, without first bargaining or haggling,
> enjoy the full delights of love and wine.
> (Faust II)

[264]Marx 1976, p. 220.

1.

In *Weltwirtschaftlichen Archiv*, issue 2 of April 1923, the bourgeois economist professor Oskar Engländer [1876–1937], Prague, demands from a modern price theory, that desires 'in some way' to go *in-depth*, two things: that it be psychologically justified and must assume the lack of own value of money (p. 283). Varga with his money that 'lost its character as a commodity with own value', meets the second demand of the mister professor. It will be shown that he, after he has repealed the law of value for gold as money, no longer is far away from also meeting the second demand, namely in place of objective regularities of economic events put psychological elements.

That the state stamped *paper note* [*Papierzettel*], which functions as money, has no own value, is undisputed. The problem is not to prove that it acts as money, *since* it is worthless, but on the contrary: to explain *why* it can fulfil this function *although* it has no own value. The attempt of Varga, to derive a money quality of the as money stamped paper chits from the fact that the gold money, which they replace, itself has become worthless – only this can be the sense of a theory of a missing own value of money, if it does not want to confine itself to the flat statement that paper money notes are worthless, – this attempt has failed.

Therefore the money quality of paper notes can and must be developed under the assumption that gold is a commodity, has value and as money is the materialisation of social labour time. The representativeness of money by paper, the valuable by the worthless, cannot be explained by equating gold, the represented, as worthless to paper. But on the contrary: paper can only represent gold as money, because gold as money has value.

Only when this conception is sharply maintained, can the laws of the circulation of paper money, both the full and the undervalued, be described.

Only in this way can under observation of the law of value, this foundation of a political economy, that sets itself the task to uncover the objective laws of the capitalist economy, the monetary theory integrate itself into the theory of the capitalist total process, as Marx has analysed it. Only in this way can the money circulation be conceived as a decisive moment in this whole process itself.

M–C–M' is the general formula of the circulation of the total capital, as it is the formula of the circulation of the single capital. M is in this formula – as also already in that of the simple commodity circulation C–M–C' –, the *hard money, gold*. Marx stresses this again and again. It is to be maintained despite all the obscuring and mystifications of the money problem by the modern normal and abnormal paper monetary system, whose mystifications also Varga

has fallen victim to. If one deviates just one step from this in the course of the examination to be proved conception, then one blocks not only the gateway to the understanding of paper money and further also the credit problem, but one gets inevitably in the vulgarism of *Say* or the utopianism of *Proudhon*. Although Marx has dealt with the one in *A contribution* and *Theories of surplus value*, the other in *Poverty of philosophy*, their ghosts, modernly dressed up, sprightly haunt through economics. For denying the own value of money is to ascribe to it in the capitalist circulation process only a formal role; to claim with Say the direct exchange of product against product as the characteristic of capitalist production, but to deny its real historical particularity: namely the necessity of the metamorphosis of the commodity into money for the realisation and appropriation of value and surplus value in money form as starting point of the capitalist total process M–C–M'! If to this merely formal mediation of the exchange of product against product by the paper money chits still is added the idea, that money without value represents the in the commodities contained labour time – Hilferding lets e.g. the value of the circulating paper money mass appear without mediation of gold as a reflection of the value sums of the to be circulated commodities –, then Say is happily complemented by Proudhon's labour money and the confusion is complete. Instead of the sharp historical-economic form determination of capitalist commodity and money circulation we have a formless mush. Instead of being able to attempt, from the money side to get to grips with the crisis of capitalism, we stand helplessly in relation to both the actual money problem and the explanations of the currency fluctuations and their influence on the figuration of the capitalist total process.

2.

In favour of the supporters of money without own value seems to speak a basic fact in the development of the modern monetary system: the credit system with its check and note circulation, its finely developed cashless payment and settlement traffic. This system has increasingly squeezed not only gold money, but also paper money out of traffic and replaced it by credit money. But the gentlemen put the cart before the horse. Because the modern credit system seems to have blotted out the last trace of gold as the basis of the money circulation and therewith the capitalist circulation, therefore money becomes for Varga, also in its gold figure, a commodity without value. The phenomenal forms of paper money circulation are taken as the laws of money circulation in general.

This is the method of vulgar economy. It does not become better thereby that the modern monetary theorists no longer, as their predecessors a hundred and more years ago, make

paper money, but credit money as the starting point of their investigations on the currency problem. For them the result of the development, the in credit system unfolded form of money already is the explanation of the money problem; instead of them deriving the laws of money circulation out of the unfolding of the form out of its basics, out of the development of gold money into the apparent opposite of itself, cashless traffic over the path of credit money. The second however is the Marxist method. It alone leads not only to comprehension of the forms of credit money, by developed from the various functions, which money assumes in capitalist circulation. It alone can above all also explain the regression of credit money into paper money occurring in Germany's monetary system. This regression in the forms of money circulation is for the crisis of capitalism in Germany just as characteristic, as with it related regression of highly-organised industrial capital into trade and usurious capital.
But if the problem of paper money in its relation with gold money is understood as the starting point for the explanation of money devaluation, then first of all paper money in its function must be sharply distinguished from that of credit money.

3.
Gold as money has in circulation two functions: that of *means of circulation* and that of *means of payment*. To these correspond two different forms of paper circulation: the actual paper money, paper money with legal tender [*Zwangskurs*], and credit money, banknotes, cheques and, in the highest sublimation of hard gold, cashless payment and settlement traffic. To make this distinction from the outset clear, is for a start important because only thus can be understood how even behind the most jolly credit building money lurks in its bodily gold figure. Then, however – this is true for the German currency questions – therefore, because today the Reichsbank notes, that is originally credit money and only auxiliary means of circulation, have legal tender [*Zwangskurs*] and under the name and appearance of credit money have become paper money in the narrower sense.
Money is a *means of circulation*, when commodities and money are simultaneously exchanged, when thus the commodity owner in the moment when he renders the commodity, becomes money owner, and vice versa. The change of position of commodity and money occurs here at the same time. This money circulates the commodities immediately.
Money is a *means of payment*, when the commodity owner renders the commodity, before he gets the money and the recipient receives it, before he pays.

The seller becomes a creditor, the buyer becomes a debtor. Since the metamorphosis

> of commodities, or the development of their form of value, has undergone a change here, money receives a new function as well. It becomes the means of payment.[265]

In the first case, the exchange of commodity against money concurrently, circulation is finished with this exchange itself. In the second case, the subsequent payment, credit relations emerge. The buyer pays only when he has sold the purchased commodity, just as its buyer. Conversely, the seller, who was yes also buyer, must satisfy his demanding men. He gives them a written promise to pay, a bill of exchange, which assures payment after a determined period in a determined legal form. This bill of exchange the receiver can swap at the Bank against notes – discounting. The notes are thus, it must be said again, *credit money*. For them do not apply the laws of actual paper money, which does not arise from credit, but rather, equipped by the state with obligation to accept [*Annahmezwang*], serve immediate circulation and spring from it. The circulation of credit money has an influence on that of the means of circulation only insofar as it co-determines their mass.[266]

From this function of the notes as from the traffic of bills of exchange emerged credit money rests for example the determination of the German law about the Reichsbank before the war, according to which the issued notes must be covered with two thirds of good bills of exchange.

GoId money, [and] even state paper money, is in high capitalism with its developed credit system has increasingly disappeared. In Germany before the war there was of state paper money only the *Imperial Treasury notes* in amount of 120 million marks; against the multiple of notes – some 2,6 billion marks in the last peace report – a dwindling amount. The capitalist, who is doing well, sees in general no more cash money. He begins his business with credit, lets his merchandise be paid cashless, he pays his interest cashless and lets the amassing profit be credited on the Bank. The full valued, covered by good trade bills covered notes are taken in traffic also as means of circulation. Gold remains in the vaults of the bank.

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[265]Marx 1976, p. 223.

[266]'I have already shown (in Volume 1, Chapter 3, 3, b) how the function of money as means of payment develops out of simple commodity circulation, so that a relationship of creditor and debtor is formed. With the development of trade and the capitalist mode of production, which produces only for circulation, this spontaneous basis for the credit system is expanded, generalized and elaborated. By and large, money now functions only as means of payment, that is commodities are not sold for money, but for a written promise to pay at a certain date. For the sake of brevity, we can refer to all these promises to pay as bills of exchange. Until they expire and are due for payment, these bills themselves circulate as means of payment; and they form the actual commercial money. To the extent that they ultimately cancel each other out, by the balancing of debts and claims, they function absolutely as money, even though there is no final transformation into money proper. As these mutual advances by producers and merchants form the real basis of credit, so their instrument of circulation, the bill of exchange, forms the basis of credit money proper, banknotes, etc. These are not based on monetary circulation, that of metallic or government paper money, but rather on the circulation of bills of exchange' (Marx 1981, p. 525).

Always 'smoother went the replacement of gold by in their natural form worthless money notes', as Varga writes, wherewith he makes no difference between notes and paper money. Gold seemed toppled from its throne. 'Money has no own value' declare the economists who take the appearance for the essence, instead of uncovering from the phenomenal forms of the capitalist process its laws of motion. But the single capitalist, for whom credit was everything and gold nothing, becomes painfully aware of the golden chain, to which he and with him the whole capitalist mode of production is bound – in the crisis. In the periodic crisis, which drives the contradictions of the capitalist mode of production to a top, in order to even them out, there occurs with the stagnation of sales the stagnation of payments. The bills of exchange among creditors and debtors cannot be cashed in, because one or the other or even all could not sell their commodities. Despite all evening out in clearing houses there remains a 'top' that must be paid cash. The bankruptcy, the crisis, makes this impossible. The chain of credit breaks. The gold chain rattles.

> Whenever there is a general disturbance of the mechanism, no matter what its cause, money suddenly and immediately changes over from its merely nominal shape, money of account, into hard cash. Profane commodities can no longer replace it. The use-value of commodities becomes valueless, and their value vanishes in the face of their own form of value. The bourgeois, drunk with prosperity and arrogantly certain of himself, has just declared that money is a purely imaginary creation. 'Commodities alone are money,' he said. But now the opposite cry resounds over the markets of the world: only money is a commodity. As the hart pants after fresh water, so pants his soul after money, the only wealth. In a crisis, the antithesis between commodities and their value-form, money, is raised to the level of an absolute contradiction. Hence money's form of appearance is here also a matter of indifference. The monetary famine remains whether payments have to be made in gold or in credit-money, such as bank-notes.[267]

The big money crisis of 1907, going out from the United States, which drove the English interest rate to an in peace time unprecedented 10 per cent, was the last example of this turning of money 'from the nebulous chimerical form it assumed as measure of value into

[267]Marx 1976, pp. 236–7. Marx adds in the footnote a point from *A contribution* (p. 146): 'This sudden transformation of the credit system into a monetary system adds theoretical dismay to the actually existing panic, and the agents of the circulation process are overawed by the impenetrable mystery surrounding their own relations'.

hard cash or means of payment'.[268] The miserable collapse of the mark support action as a last symptom of the complete collapse of the German monetary system hammers home even to those who hitherto did not want to see: that behind all paper and credit money gold stands, gold, that is to be cherished and cared for.[269] The mark supporting action however pumped gold from the Reichsbank, devalued thereby the paper money even more and thus proved negatively, that gold only for the devout Christian is a thing, which moths and rust eat, but for the capitalist economy it is the soul of business.

4.

German paper money, that in these days has reached the lowest level among all ever in capitalist states fabricated paper chits, originates from credit money, the banknote. If the latter has also assumed the function of means of circulation, after being in principle a means of payment, then the former serves in principle circulation, to satisfy the credit need of the state.

When by the law of 1 June 1909 the banknote alongside gold was declared legal means of payment in Germany, when simultaneously the issue of notes of 50 and 20 mark, instead of hitherto 100 mark, 500 mark, 1000 mark and a multiple of 1000 mark, was permitted,[270] the state sanctioned what money circulation actually already long had developed: the use of banknotes also as means of circulation. Because the banknotes fulfilled and could fulfil their function as credit money, so long as German capitalism still developed upwardly, they could also share in taking on the function of paper money, without being paper money. The declaration of credit money as legal means of payment alongside gold, so that for example since then all wages and salaries could be paid also in banknotes, instead of hitherto only in gold, served the purpose of strengthening the gold treasure of the Reichsbank, as paper now could represent gold money in circulation in still larger dimensions than before. The law belonged thereby to the financial armament of imperialist Germany and was so the first step

[268]Marx 1987, p. 378.

[269]In the same number of *Weltwirtschaftliche Archiv*, in which mister professor Engländer denies depth to any theory which does not assume the missing complementary value of money, Mr professor Lewinski from Warschau says: 'On the goal of our currency policy there appears today to exist full agreement. The attacks directed against the 'gold craze' have fallen silent and all efforts are directed to restoring, in the more or less distant future – corresponding to the economic situation of the different countries – the once by many theorists contested gold currency. As stated: this stands in one and the same number, one and the same journal together with the excommunication that Mr Engländer hurls against all those that suffer from 'gold craze'. – A contribution to the theoretical dismay which the gold and currency problems still today spread in vulgar economy. But for the solution of the currency confusion it is not a matter of theoretically destroying the gold craze. It is a matter of re-introducing the gold currency. The where and how is the decisive question here. On it also mister Lewinski gives no answer with all historical knowledge of previous money troubles.

[270][In France too banknotes were made legal tender a few days before Germany, also in anticipation of war. For the same reason the introduction of small denomination banknotes was opposed by Karski 1913a.]

toward currency devaluation.

When by the law of 4 August 1914 the Reich was authorised 'in order to cover the extraordinary credits' as a result of the war to issue bills of exchange, when it was further determined, that these bills of exchange were to be equated to trade bills as coverage for the note circulation of the Reichsbank, and when finally it was arranged that token coins and notes could be redeemed not by gold, but also by notes, then with one stroke both economic foundations of note circulation as credit money were smashed.

Of course since 1909 the banknote, as it became legal means of payment, had obtained functions of means of circulation. But its basis was and remained the *trade* bill, that in turn went back to the capitalist circulation M–C–M' actually taking place. It *replaced* gold, insofar as the credit demands evened each other out in circulation. It *represented* it until its at any time possible redemption in gold, insofar as and until after successful balancing out the remaining amount of money was to be paid in gold. Henceforth the *finance* bill of the Reich, behind which nothing stood than the daily further dwindling credit, than the hope of *Helfferich* that the Frenchman will pay, became the decisive gauge for the scope of the note issue and the almost exclusive foundation of their coverage.

Certainly also after 4 August 1914 and still today there stands on each Reichsbank note the solemn promise of the Reichsbank directorate, that 'the Reichsbank's main treasury in Berlin for this banknote to the deliverer' pays its denominated value. But the deliverer of a note of 1000 M. receives no longer, as formerly, fifty 20 mark *coins*, but – after preference – ten 100 mark-, or twenty 50 mark-*note* [*scheine*]. Thereby the obligation of convertibility of the notes by gold is suspended. The banknote holds [*gilt:* counts] no longer 'in lieu of gold and pearls'. It holds in lieu of other paper notes [*Papierzettel*].

It no longer serves as a means of circulation *alongside* gold, which does not yet necessarily cancel its character as credit money. It has *become paper money, exclusively a means of circulation*.

If the law of 1909 *confirmed* merely a development accomplished in money circulation itself, then the law of 1914 *changed* the function of banknotes: it turned them from *bank* notes into *state* notes. The ambiguous character of the notes that they had already previously assumed, when they except as means of payment also functioned as means of circulation, remained with them even after 4 August 1914 because also still now trade bills of exchange served alongside Reich bills of exchange [*Reichswechseln*] as cover for the note issue. But they decisively changed their character: the notes as means of circulation, the state notes, increasingly outweighed the notes as means of payment, the bank notes, the more [that the]

finance bills of exchange supplanted the trade bills of exchange.[271] Credit as the exclusive basis of credit money broke the neck of credit and of its [kind of] money. In place of the laws of circulation of trade bills and their notes stepped forth the laws of inconvertible [*ungedeckten*: unbacked] paper money.

Wilhelmine Germany, when it transformed the banknotes into state notes, did the same thing as England had done during the Napoleonic wars when it from 1797–1823 eliminated the convertibility of the notes of the Bank of England, or as the United States when they in 1861 with the outbreak of the war of secession likewise cancelled the obligation of note convertibility. Then as now the prompt onset of paper money depreciation, which in England 1814 reached up to a gold agio of 30 per cent, in North America up to 185 per cent, taught that the state power could undoubtedly print money, but not make money.

The theory of money without value fails always then when it should realise itself in practice. Every time the printing press should replace the coinage stock, gold makes its in the capitalist economy inalienable claims.

5.

What are then the laws of paper as a means of circulation, which have enforced themselves in England, in the United States and in Germany as in Poland and Austria to the chagrin of the money creators always then, when they most needed the note press? What are the relations between gold as money and paper as a means of circulation in their qualitative and quantitative determinedness? From what causes and to what extent can paper step into circulation 'in lieu of gold'?

We again come to the question, which is the core of currency problem.

For Varga paper is *replacement* of gold money. From his standpoint of the worthlessness of money, his assumption that gold and paper mutually 'replace' themselves, so that one can stand in the place of the other, is only consistent. But this 'replacement theory' is firstly inaccurate: it does not distinguish between credit money, where the money replacement by

[271]Soviet Russia shows an inverse development from state note to banknote. There alongside the *state note*, the *banknote,* on gold ruble basis, is developed systematically and strictly separated from it. The Soviet ruble is pure state money, means of circulation. The banknote, the *Chervonets*, is credit money. It is issued against gold trade bills. Moreover there exists a gold coverage of now 49 per cent of the note circulation. The Chervonets is full valued (see Heichen 1923). Heichen remarks: 'That the state bank supports and encourages the bad money economy of the private economy ... by granting credit, like this happens on the part of the German Reichsbank just as on the part of the Polish agricultural central loan association [*Landeszentraldarlehnskasse*], such an idyll for private economic surplus-making on the basis of money depreciation differences no longer exists in Russia'. – In Germany conversely this private surplus-making is sanctioned by the foreign currency exceptional decree of 22 June, when by concentrating the foreign currency business in the hands of the big banks all profits from foreign currency speculation are shovelled to them thanks to the authorities. The question of the shifting of the currency risks is exactly a question of political power, that only with the means of the revolution can be resolved in favour of the proletariat.

notes to some extent is possible, and paper money. Secondly, it is theoretically wrong: it is contrary to the law of value. Thirdly it is refuted in practice: the mark support operation has lead all replacement theories to absurdity.[272]

The principle of paper circulation is: Paper can come as money into circulation, because and insofar as gold is necessary, to undertake the metamorphosis of commodities into money. Paper money does not *replace* gold in circulation, but represents, symbolises it. In other words: When C–M–C following the law of value is the exchange of equal values, that is M as gold, money, contains just as much social labour as the C to be circulated by it, then paper can take over the circulation function of gold, because and insofar gold at any time can again circulate in its place. Gold can change itself out of its money figure therefore and to that extent into paper, as paper can again be converted back into gold.

In these sentences is established the on the law of value build theory of paper money as means of circulation.

> Paper money is a symbol of gold, a symbol of money. Its relation to the values of commodities consists only in this: they find imaginary expression in certain quantities of gold, and the same quantities are symbolically and physically represented by the paper. Only in so far as paper money represents gold, which like all

[272]A reversal of the theories of missing own value of money is the teaching of Helfferich of 'functional value' of money. For him the value of money – he is an opponent of worthlessness theories – can under certain preconditions exist independently of the value of any one money material: 'If with paper currency the material, of which the money consists, is worthless, if further the paper slips do not include any right to demand a valuable material, then the paper money nevertheless has, so long as it is accepted in exchange against some other object of commerce, a value changeable in relation to all other values and therewith a value independent of all remaining value objects, which can rest exclusively on its function as money' (Helfferich 1921, pp. 535–6). – While thus the theorists of the lack of an own value of money remove the value from gold as money, because it can be 'replaced' by paper, Helfferich gives paper money value because it as a means of exchange functions just as the 'due to its material value-full' gold. Helfferich derives the functional value of money from its function of means of exchange and comes thus to the value of as money functioning chits independent of its 'material value'. In reality however gold conversely becomes money, a means of exchange, because it has value; and the problem of paper money consists precisely to understand its function as money, *despite* the fact that it as paper chits has no value. This can only happen, if its relations with gold are pointed out. – The quid pro quo of H. stems from his value conception, which is the the usual vulgar-economic 'the relation of the subject to the things of external world'; which relations make themselves felt in the need satisfaction and the restrictions corresponding to them to be overcome by 'labour and sacrifice'. This value conception not only conjures away any objective value theory but also with the functional value of money its intrinsic value, which it has in its gold form as a commodity, as product of human labour. Thus for H. despite all functional value the paper money problem remains an unsolved riddle: 'Insofar as the money provision proceeds by the issue of paper slips, a general statement cannot be made, since the extent and the change of the money provision here depends on the policy of the state, which emits the money slips' (p. 548). The policy on which the State Secretary of finance promoted professor Helfferich set all root, was Ludendorff's victory. When the latter's sabre became notched, together with the finance practice of H. also his theory collapsed. Its leftover is the grotesque claim of H. in the mark support committee, that in Germany there is no inflation. One knows, even when one is professor of economy, finance minister, bank director and Deutschnationale representative in the Reichstag, about paper money 'nothing certain'; and for the rest it has 'functional value'.

> other commodities has value, is it a symbol of value.[273]

As gold with the development of the commodity economy originally became money, so develops with the deploying commodity economy originally the representativeness of gold as money by notes, symbols of gold money. The gold coin wears off in traffic. Its weight and therewith its value becomes lower by the performance of its means of circulation function, than what it said at its minting. Which for example the German coinage law recognises thereby that it takes away the property of full-valued gold coin from gold coins that fall below a certain weight, the tolerable weight, 1/5000th of the legal weight in case of the 20 mark coin. Within these limits also a no longer full-valued gold coin can be accepted as full-valued; it thereby becomes a symbol of the full-valued 20 mark coin. Thus already circulation makes the gold coin into a sign of itself, into a *value token*.
Varga describes this formation of the value token inaccurately and lopsidedly:

> By legally determined division of gold in certain fixed quantities that in minted form come into traffic, the immediate relation between gold as measure of value and the gold quantities as standard of price is slowly blurred. The coin maintains its own name, figures as such in the circulation. This gives the possibility, the replacement of gold as means of circulation by paper money notes [*Geldzeichen*].[274]

The theoretical representation, which, as always with Marx, is only the ideal reflection of economic historical development, goes precisely in the opposite way. The special denomination of the coin, that is the separation of its name, which is originally a weight name, from its real weight is first a consequence of the below-weightedness emerged by abrasion in the fulfilment of the circulation function of gold and the despite this below-weightedness continuing circulation of the coin as a full-valued one. It is the *consequence* of the symbolisation of gold through tokens of itself, not its *cause*.[275] It can therefore not be used for the explanation of the paper money problem.
The legal fixation, the denomination of the state, takes place only after the commodity traffic has set all economic preconditions for the coin baptism, but has also for coin forgery, whose last example on a scale of billions is the German paper money swindle.
If already the gold coin in circulation becomes a representative of gold money, then

[273]Marx 1976, p. 225.
[274]Varga 1923, p. 145.
[275]See Marx 1976, p. 194.

therewith the possibility is fundamentally explained of the replacement of gold by other signs [*Zeichen*: tokens]: token coins [S*cheidemünze*: small change], paper:

> The fact that the circulation of money itself splits the nominal content of coins away from their real content, dividing their metallic existence from their functional existence, this fact implies the latent possibility of replacing metallic money with tokens made of some other material, i.e. symbols which would perform the function of coins …
> In its form of existence as coin, gold becomes completely divorced from the substance of its value. Relatively valueless objects, therefore, such as paper notes, can serve as coins in place of gold. This purely symbolic character of the currency is still somewhat disguised in the case of metal tokens. In paper money it stands out plainly. But we can see: "*Ce n'est que le premier pas qui coûte*" (everything depends on the first step).[276]

'But the second step brings something new' – complement the Helfferichs and their successors, the French proverb and print diligently paper money, after having through a stroke of the pen changed banknotes into state notes.
But alas: paper money is not gold *replacement*, but gold *symbol* and as such bound to the same strict laws in circulation as the by it represented gold, when it would circulate itself.
Gold, if it circulates, cannot in a random amount revolve. But the amount of the revolving gold is precisely determined by the laws of circulation itself, which again run back to the law of value. Marx formulates the general law, that determines the mass of as means of circulation functioning money, then:
(sum of prices of commodities) / (velocity of the same named money pieces) = mass of as means of circulation functioning money
This law is readily apparent. Are for example in one day commodities to be circulated for 100000 marks (sum of prices of commodities) and if any 20 mark piece revolves ten times on that day on average (velocity of the same named money pieces), then there are five hundred 20 mark pieces required to change the 100000 marks from their commodity form into the money form.
This law then, that determines the mass of gold money necessary for circulation – abstracting here from its modification by credit money –, also determines the limits within which the paper money as a symbol of gold can revolve, so precisely, that any violation of

[276]Marx 1976, pp. 222–4.

these limits draws the penalty of paper money devaluation to itself.

From what has been said it follows: even with highly developed credit relations there must always revolve a certain minimum mass of gold – provided a 'normal' capitalism – alternatively to fulfil the not offset payments, and to carry out the innumerable cash purchases. This minimum mass of gold required for circulation, that is definite by experience, can be represented with full validity by paper money.

The minimum of gold, that the circulation needs, is simultaneously the maximum for the paper money to be issued. Once more paper money is issued, it depreciates against gold.

This scale-relation, that derives from the above specified formula, is, though also not expressed numerically, nevertheless an objectively exact magnitude – just like the value-relation [*Wertbeziehung*]. Like the latter it sets itself through behind the backs of capitalist production agents. That the scale must be kept, if the paper money is not to become below value, is only brought to consciousness to the capitalist society first by the violation of the scale, by devaluation of paper money. The exchange rate tables of the market cast the most painful book on each violation of scale.

The scale, is, insofar as modern capitalism knows paper money at all, empirically observed by it either through the limitation of paper circulation to a sum remaining far behind its upper limit, for example to 120 million marks with the Imperial Treasury notes [the case prewar], or by the possibility of convertibility of paper against gold; so that the representativeness of gold by paper is secured thereby, that gold always can take the place of paper.

But as soon as paper money with forced currency [*Zwangskurs*], that is real paper money, is issued and simultaneously, which therewith tends to go hand in hand, the limitation of its issuance lifted, the capitalist state itself blocks the safety valve that protects it from paper money depreciation. Paradoxical as it may sound: the laws of the circulation of paper money as gold symbol can only by the most ruthless suppression of paper money be maintained. In the moment, when it absolutely accesses the reign, its depreciation begins.

6.

After the war legislation in Germany had torn down the mechanical limit protections against the depreciation of paper money, the latter has in ever more stormy pace set itself through. Germany has from a country with highly developed credit money become the type of the country with pure paper currency. It suffices to counter-pose the note circulation of 30 June 1914 and of 7 June 1923, to make comprehensible the fall of the mark into the abyss. On 30

June 1914 at a gold stock of 1,306 billion marks and a bills of exchange and cheque stock of 1,212 billion marks there circulated 2,406 billion mark notes. On 7 June 1923 with a gold stock of 756.9 million marks in the vaults of the bank and 180 million marks abroad as well as a bills of exchange stock of 4.6 trillion marks and interest-bearing treasury certificates of 8,448 trillion marks the circulation of notes and Loan Bureau Certificates amounted to 9,312 trillion marks. Until 15 June 1923 the note circulation has risen from 1595.5 billion marks to 10.9 trillion marks. In the Ruhr war the Reich continues the war-finance-policy: to cover the money need of the state with treasury bills of exchange [the so called *Reichsschatzwechsel*] and issue therefor notes. The floating debt of the Reich, which through the by treasury bills of exchange covered, though not secured notes is mobilised, was on 10 June 11,483 trillion marks, 1,568 trillion mark more than on 31 May. Gold shows an opposite movement: it has since 30 June 1914 decreased to 370 million marks, while the paper circulation has increased more than four thousand fold. Simultaneously in place of trade bills of exchange stepped mainly the finance bills of exchange of the Reich. The result is that the 10000 mark note is worth 25–30 gold pennies.

The question, *for which reason* it came in Germany to this credit economy of the state and to depreciated paper currency, for which reason Germany covered its credit essentially with the note press, while England for example had an entirely different system of war financing by taxes, is with the enumeration of these data not yet answered. The examination of the economic causes of the German war and post-war fiscal policy does not belong in the frame of this work, which only wants to analyse the events of circulation.[277]

The movement of paper separates itself from gold. Paper money seems to make itself independent of gold money.

From the servant of circulation it becomes their lord. As a representative of gold paper steps forth in circulation in order to completely eject it from it. If gold was money, because it is commodity, then paper money becomes a commodity, because there it is money: From an instrument and goal of profit and speculation money becomes in its paper figure their object. Its depreciation determines the economic cycle and employment level [*Arbeitsmöglichkeit*: labour opportunity], rather than the economic cycle and labour opportunity guaranteeing its full valuedness:

[277]For the same reasons also the in general important repercussions of money depreciation on the organic composition on the in Germany active capital are not examined. In the essay 'Die Geldentwertung' [Money depreciation] (1922) I have attempted to give a representation of this problem in connection with the over-foreignisation and denationalisation of German capital. [German capitalists place their money abroad (in the Netherlands, Switzerland, Sweden), demand payment in foreign currencies like the dollar also on the domestic market, convert their money into foreign currencies, join foreign holding companies, and through them buy capital in Germany.]

> In the circulation of tokens of value all the laws governing the circulation of real money seem to be reversed and turned upside down. Gold circulates because it has value, whereas paper has value because it circulates. If the exchange-value of commodities is given, the quantity of gold in circulation depends on its value, whereas the value of paper tokens depends on the number of tokens in circulation. The amount of gold in circulation increases or decreases with the rise or fall of commodity-prices, whereas commodity-prices seem to rise or fall with the changing amount of paper in circulation. The circulation of commodities can absorb only a certain quantity of gold currency, the alternating contraction and expansion of the volume of money in circulation manifesting itself accordingly as an inevitable law, whereas any amount of paper money seems to be absorbed by circulation. The State which issues coins even 1/100 of a grain below standard weight debases gold and silver currency and therefore upsets its function as a medium of circulation, whereas the issue of worthless pieces of paper which have nothing in common with metal except the denomination of the coinage is a perfectly correct operation. The gold coin obviously represents the value of commodities only after the value has been assessed in terms of gold or expressed as a price, whereas the token of value seems to represent the value of commodities directly. It is thus evident that a person who restricts his studies of monetary circulation to an analysis of the circulation of paper money of legal tender [*Zwangskurs*: forced currency] must misunderstand the inherent laws of monetary circulation. These laws indeed appear not only to be turned upside down in the circulation of tokens of value but even annulled; for the movements of paper money, when it is issued in the appropriate amount, are not characteristic of it as token of value, whereas its specific movements are due to infringements of its correct proportion to gold, and do not directly arise from the metamorphosis of commodities.[278]

With these sentences Marx has not only dealt with the quantity theorists[279] and vulgar

[278]Marx 1987, p. 356.

[279]Varga in the 'economic report' for the first quarter of 1923 (*Inprekorr*. No. 68) polemicises from the standpoint of paper circulation against the quantity theory: 'Theoretically interesting is the fact, that in the same period, when the mark was maintained stable by the support action, the note circulation has increased by thousands of billions; this is a palpable proof, how false the quantity theory is, which makes the currency exchange rate [*Valutakurs*] and prices directly dependent on the total sum of the note amount placed in traffic' (p. 549). This is at the least inaccurate. If one regards only the paper money movement, detached from gold, as Varga does here, then the quantity theory seems correct. The increased paper money issue draws necessarily in its wake the intensified paper depreciation, which manifests itself in the rise of prices. If with the mark support

economists of his time, but also disposed of their descendants. Whether they swear to the theory of missing own value or to that of the functional value of money, or even, dressed up in Austro-marxist fashion, render homage with Hilferding to the theory of the social circulation value of paper money:[280] all take the peculiar motions of paper circulation for the general laws of money currency.

7.

The false appearance, as if the phenomena of paper circulation were the rules of money circulation, vanishes as soon as the borders of the state are traversed, in which a paper economy prevails. Paper money is state money. As the uniform of the soldier holds only in the homeland, that he should defend, so the state stamped paper holds only within the border post, whose coat of arms it carries. Beyond the borders must be paid in cash. World money is gold.

May the vulgarus take the appearance for the essence when he for the movement of the paper

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action this did not immediately set itself through, then this was due to the the political measures of the government, which admittedly by the growing note flood soon were thrown into disarray. Meanwhile the new price surge can have convinced also V. of the untenability of his view. – The quantity theory can only be confuted when the close dependency of paper money value on the gold circulation is shown. While thus V. comes for gold to the consequences of the quantity theory (see above, pp. 337–8) he polemicises here against them from a wrong position.

A particularly beautiful variation of the quantity theory is incidentally that most widespread explanation of the paper money mystery, which sees in the paper notes an 'additional' purchasing power, that make themselves felt on the market and that increase the prices. – This statement is at approximately the same scientific level as the medical diagnosis by Sganarelle in Molière's *Le Médecin malgré lui*: 'Your daughter lost her speech from impediments to the action of her tongue'.

[280]Hilferding's 'social circulation value of paper money' (1981, pp. 28 and following) is nothing more than the Austro-Marxist twist of the vulgar economic 'functional value' of Helfferich. The value of the circulating paper money is determined for him no longer, as in Marx, according to the relation of paper money mass to the in circulation required gold as money, that represents this, but immediately from the value of the commodities according to the formula:

(Sum of values of commodities) / (money velocity), plus the sum of the payments due, minus the offsetting payments, minus the number of exchanges, wherein the same piece of money alternatively functions as means of circulation and means of payment, = the sum value of the circulating money, regardless whether it is gold money or paper money.

In Marx what is decisive for the *mass,* not the *value,* of the circulating gold is not the *value* sum of commodities, but their *price* sum, that is their value, already measured and expressed in quantities of gold, and therefore directly related to gold as a commodity and as money. From this Marxist formula results immediately the minimum for circulation required gold, which is the scale for the paper money issue. When Hilferding aggregates the value sums of the commodities, without relating them in advance as prices to gold, he deactivates gold as a measure of value for the commodities, as well as for paper money: 'The real measure of value is not money, but the “exchange rate” [*Kurs*] of money is determined by what I would call the social circulation value'. (Follows the formula p. 29.) This 'course' of money however, which assesses the commodity values and in this way first becomes a reflex of the commodity values, is the 'functional value' of Helfferich. According to Helfferich money has value because it functions as a means of exchange. According to Hilferding it has a 'course' because it 'circulates' and turns over commodities, thus likewise functions as a means of exchange. – Helfferich denies the inflation. Hilferding gave the Cuno government the practical advice resulting from his theory, of reducing the paper money mass by throwing gold in circulation, to distribute the reflex of commodity values on to a smaller paper money mass. The gold is gone, the paper money flood risen. Hilferding can become reconstruction minister. [Hilferding in fact became finance minister on 14 August.]

chits of his country demands general validity: world capitalism insists, that the appearance gets honoured in the commodity, that everywhere has the right of domicile, with gold in its natural figure, in by weight measured bullion.

Varga tries also for gold as the world gold to show the tendency of its replacement by paper. Following a quote from Marx,[281] in which he points with all stress to the role of gold as world gold, Varga continues:

> In fact before the war in international traffic likewise money tokens – notes, foreign currencies – served as international means of circulation.[282]

Besides the fact that the notes and foreign currencies are credit money, means of circulation, not paper money: What is up with this type of Marx improvement? A glance in *Capital* would have convinced Varga thereof that Marx no doubt knew the role of credit money in international traffic. Would Marx really have known nothing of bills of exchange, the century-old international credit money? What matters after all is again only this: that the claims and debts not mutually compensated in international traffic of the capitalist states are balanced out in gold – that the paper slips of one state do not hold in another, when gold does not stand behind them.

Credit is translated only by the *vulgarus* with 'confidence'. For the capitalists in world traffic it is an objective parameter, that itself is best assessed in gold. Only a capitalist country that has gold, has credit, has full valued foreign currency and notes in international traffic. But gold has a country then, when it has an active balance of payments. The question however of the active balance of payments is no longer a question of only circulation, national and international, but a question of the reproduction of the single national total capitalisms. At this point the phenomena of circulation switch into the movement of the reproduction of the total capitalism.

At the border, where the money note loses its value, when it is not gold plated, emerges not only the difference of the internal and external value of the under-valued paper money, the source of currency profit and a cause of illusive conjuncture cycles,[283] there is revealed with the health of the paper money also the degree of the health or disease of the capitalist economy standing behind it.

At the same time gold destroys, when it as world money makes the conditions of existence of

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[281]Marx 1976, p. 105.
[282]Varga 1923, p. 147.
[283]See Ludwig 1922, pp. 133 and following.

world capitalism felt to the capitalism of individual countries, with the external depreciation of paper money its value also in each emitting state, verifies to it its attachment to gold precisely thereby, that gold wanders off.

This interaction between the internal and external value of paper money in their common reduction to gold cannot be comprehended by those who do not recognise gold as a commodity as the foundation of paper money.

Only from this false conception could the conception arise that through the finance-technical means of the mark support action, except a temporary speculation effect, a permanent or also just temporary stabilisation of the mark could result. Only who, as Hilferding or Helfferich is of the opinion that money has value, because it functions as a means of exchange; only who thus derives the value of money from its function, not its function from the commodity value underlying it, could believe that it would suffice to buy paper with gold, to stabilise the mark. For this position is indifferent towards the commodity quality of gold money; according to it paper as money has independent value, which is increased, when another 'money material' reduces the amount the paper.

In truth however the mark support action, which proceeded in the form of a currency stabilisation attempt, was nothing else than the elementary evening out of the balance of the payment, the payment of debts of the German total capitalism to its capitalist creditors abroad with world money, gold, or gold-valid credit notes [*goldgeltenden Kreditzeichen*], foreign currencies.

When the German Government under the coercion of the Ruhr war cheapened the dollar price, it gave the German coal and raw material importers cheap means of payment, with which they paid their English and American debt. When it expended gold from the Reichsbank, to buy German mark notes in New York and Amsterdam, it paid with gold the in these mark notes securitised claims of American or Dutch owners of German paper-owners, it evened out with gold the passive balance of payment.

The result was the opposite of that what otherwise is the precondition of any mark stabilisation: the outflow instead of the inflow of gold, the planless multiplication instead of the systematic reduction in paper money circulation. The balance of payment was being evened out. The value of paper money was being further destroyed.

So the result of the mark support action reveals again only the dependence of the circulation of money on gold and simultaneously the inner connectedness of the internal and external value of paper money. It shows simultaneously that the circulation phenomena do not exist by themselves, but in their workings are symptoms and moments of the reproduction of the

total capitalism.

Therewith the examination of the currency problem flows into the critique of the political economy of world capitalism in its contradictory development [*Ablauf*].

Chapter Sixteen

The Problem of Gold Inflation in the United States (15 November 1924)

Karl Korsch

Critical marginalia to comrade Varga's theoretical remarks in the latest economic report of *Internationale Pressekorrespondenz* (3 November, pp. 1883–4).

It does not belong to the tasks of comrade Varga, in his periodic economic reports on such problems, like the problem of the so-called 'gold inflation', to take theoretical position from the Marxist standpoint. If however in our *Internationale Pressekorrespondenz* on such a question a theoretical position is taken, then one would have to expect and desire, that this theoretical statement happens on the basis of Marxism. The opposite occurs in these 'theoretical' remarks of Varga on the problem of gold inflation. He criticises not the pseudo-problem of the so-called gold inflation from the standpoint of Marxist theory, but he attempts obversely to criticise the standpoint of Marxist theory through the development of an in his view really existing problem of gold inflation. Already a quick glance shows, which is then confirmed by extensive analysis, that the apparent main purpose of these 'theoretical' remarks consists, of combatting and disproving certain basic teachings of Marxism (the law of value, the commodity character of money) from the standpoint of bourgeois vulgar economy and the in light of this science viewed 'reality'. Of course this attempt by Varga just like, all his more or less famous predecessors, failed completely. But this failure must be critically substantiated. And besides, the mere fact that such an attempt in such an important journal as *Inprekorr* by such an important author as Varga has been undertaken at all, makes an extensive critical analysis of this attempt an absolute necessity.

We declare in advance that *our critical analysis solely relates to the statements of Varga, which he in his economic report explicitly designates as in a special sense 'theoretical' and therewith has separated from his other statements* (p. 1883: 'Theoretically interesting is here the following' and so on). With the statements of the *economic statistician* Varga and the *descriptive economic historian* Varga we have here no beef. On the contrary, we will have in the course of our critical analysis of the economic 'theorist' Varga multiple occasion, to base ourselves on the statements of the economic statistician Varga, in order thereby to refute Varga himself. And we will by this division of the one, ostensible unitary Varga in several different and one another contradicting Vargas do no injustice to Varga. His own

statements reveal clearly: Two souls, alas, reside within his breast. The one is the peaceful soul of the sober and economic reporter, who says with Wagner: True, I know much, but want to know it all. Alongside it dwells however the wild, Faustian soul of the economic theorist with its debauchery in the realm of 'theoretically interesting' remarks. The economic correspondent Varga reports in a completely calm and objective fashion about the really existing conditions and events, and it is not his fault, when the economic 'theorist' Varga interrupts him with his 'interesting' remarks on some 'problem'.

So steps forth in the short article of Varga's latest economic report, which here is discussed and which Varga has given the heading 'The problem of gold inflation in the United States', clearly the author Varga in both his different character masks. The 'theorist' interrupts the correspondent unburdened by theory, and the whole article is divided thereby also externally in three different, with each other only loosely connected and to some extent even contradictory parts. The *first* part is statistical and treats, despite its misleading heading, not at all of a 'gold inflation'. The economic statistician Varga numerically observes therein that the gold stock in the United States since a long time shows a great and still increasing tendency to rise. Also the *third* part of the article (introduced by the words 'From the economic perspective the question namely stands like this'), treats not at all of gold inflation. The economic historian Varga gives therein a fine and concise overview of the different, successive and with each other intertwined forms, in which within the last ten years the development of the United States 'from a colonial country to an imperialist power, which itself invests capital abroad and exploits foreign countries', has come to light in economic phenomena. In between these both parts however a *middle* part squeezes itself. In it takes the word, quite abruptly, the economic 'theorist' Varga and presents us with those 'interesting' considerations, which constitute the particular object of our critical analysis.

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The theorist Varga begins his remarks with an *excursion to the future*. The statistician Varga has reported that in the first eight months of the year 1924 an enduring 'gold flow' increased the gold stock of American banks to such extent, that at present already a quarter of the total circulating money consists of gold and hundred per cent backed gold certificates (p. 1883). He added that in the latest month report (September 1924) admittedly stagnation set in. The surplus import of gold in this month has despite the great active balance of trade (at a level of around 140 million dollars) fallen compared to August from 15.8 to 1.6 million dollars. Varga believes however, that this phenomenon occurring for the first time in years is only 'a temporary phenomenon caused by the great foreign loans' (p. 1883).

The economic theorist Varga now envisions that this great and still increasing stock eventually can grow so much, that circulation 'may' be transacted entirely by gold, respectively hundred per cent gold certificates, and asks, what actually would happen, if then 'still further gold accrues'. Further below he thinks that the herewith given question of 'gold inflation' presently to be sure however is still not acute, but that there are nevertheless also 'people' who 'are of the opinion', that in the United States gold inflation already exists. And 'in any case' the amassment of gold already today gives 'American economists great worry' and is 'a special impulse of the imperialist-expansion-yearning of the United States'. In another place (after the description of both, in his view only possible phenomenal forms of the impending American 'gold inflation') he opines that 'in both cases severe disturbances of the economic life will be the consequence'.

Already in this place, still before we learn in detail of the by Varga developed phenomenal forms of gold inflation, that would refute the Marxist law of value, the Marxist reader must interrupt the 'theorist' Varga: But how do things stand, comrade Varga? You after all have yourself on the preceding page (last footnote to the previous article, p. 1883) poured your justified scorn over the 'bizarre idea' of the 'supporters of the class harmony theory', who 'by the regulation of monetary circulation, by the manipulation of the medium of circulation want to manage the whole course of production'. Even more baseless than such practical ideas, which, applied as experiments, at least in their subsequently resulting fiasco find a certain type of 'realisation',[284] your after all purely theoretical idea, that such disturbances of the monetary circulation, like the so-called 'gold inflation', as their 'consequence' must bring forth such 'severe disturbances of economic life', that in the hereby stirred 'great worry' of 'American economists' a 'special impulse of imperialist-expansion-yearning of the United States' must be seen.

Little causes – great, all too great effects! It does not occur to us to claim, that certain 'disturbances of economic life' could not also in reality one time be induced as a 'consequence' of an in the circulation sphere occurred disturbance. We hold with Marx, who explains, that 'from the fact that the popular ascription of stagnation in the processes of production and circulation to an insufficiency (or superfluity. K. K.) of the circulating medium is a delusion, it by no means follows, that an actual shortage of the circulating medium resulting from, say, bungling government interference with the "regulation of currency" may not for its part give rise to stagnation'.[285] But with all this the 'delusion' remains a delusion, and a vulgar economic representation a vulgar economic representation.

[284]See Marx 1987, p. 414.
[285]Marx 1976, p. 218.

Varga has in his capacity as economic historian, in the third part of the article, clearly and correctly noted the real, enduring 'impulse' of imperialist development of the United States: the enormously grown production (more than half the world production of the most important commodities), necessity to export without corresponding actual import needs (about 20 billion dollar of commodity export in excess over import in the last ten years). Why then still this vulgar psychologising 'special impulse' for imperialist 'expansion yearning' of the United States in the form of the 'great worry' of American economists' due to the 'severe disturbances of economic life' as a result of threatening 'gold inflation'? Chapman's associate Samuel Gurney did not know such worries: 'All fluctuations in trade are advantageous to the knowing man'.[286]

Our further investigations will show that already the until now considered, still somewhat secondary errors of the 'theorist' Varga are not at all an accidental lapse, but the necessary consequence of a vulgar-economic basic conception.

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Let us move to the essential. Varga, the economic historian, presented us in the third ('economic') part his explanations, of the different economic 'phases' of that great, at present not yet closed development process, through which the previously capital importing colonial country developed into a capital exporting colonising power. That this process is not yet closed, a general, international stabilisation of the new relations not yet achieved, prove clearly the different phenomena, which the economic historian Varga has carefully recorded: the existence of inter-allied debts, of which until now only the English are being paid and redeemed, – the despite a 'temporary' interruption in September also further enduring 'flow of gold' to America. The economist Varga has also clearly shown in which direction these still unfinished economic phenomenal forms of imperialist hegemony of America already now tend to seek their consummation: in the 'investment of excess amounts of capital abroad, that is purchase of securities, which secure a part of the surplus value which is produced in foreign countries'. He has in a specific article (pp. 1884–5) portrayed the forms of this foreign capital investment.

What has Varga, the economic 'theorist' (if we still want to maintain for a moment the already by him, not by us, created division of *unitary* political economic theory into economic history, economics and 'theory'), to add further to this economic historical and economic description of the factual events by way of 'theoretical' remarks, to understand these immediate phenomena of the economy as a Marxist and to make them understandable

[286]Marx 1981, p. 549.

in a Marxist way?

It is entirely self-evident, that such an enormous and at present still by far not completed development process, like the development of America to dominant imperialist power, in an economy, which is not a consciously and by plan regulated *labour economy*, but a quasi-natural rough-and-ready and *post festum* itself regulating capitalist *commodity economy*, can take place only under manifold and enormous contradictions. It would be a magnificent task for a Marxist, to critically develop these *real contradictions* and simultaneously the *imaginary forms*, in which they are reflected in the consciousness of their agents and their economic 'science', and to show, how throughout all these contradictions and in these contradictions themselves the basic law of Marxist economy, the law of value, realises itself. The 'scientific' theories and popular representations about the so-called 'gold inflation', together with the real contradictory phenomena, which find in these theories and representations their still greater contradictory expression, would in this context have to be treated as something like Marx in the first volume of *Capital* has treated Nassau W. Senior's 'Last Hour'.

Varga unfortunately has put himself with his 'theoretically interesting' considerations an entirely different goal. One must not let oneself be deceived by a few Marxist expressions (like surplus value, exploitation, and so on), which the 'theorist' Varga occasionally kneads like raisins into his dough. The real intent of his 'theoretical' explanations about the problem of gold inflation is that he wants to disprove the Marxist theory of the commodity character of money, which constitutes an indispensable component of the Marxist value theory, and therewith thus this Marxist value theory itself. Partially his attack is aimed also directly against 'the law of value' (as the law of the exchange of equal quantities of labour time). And we will see that also the method employed by Varga for his 'refutation' of Marxism has still remained the unchanged same, as once Bernstein and other 'refuters' of Marxism have employed. His whole theoretical play consists of repeating a few, old, already by Marx himself as absurd proven sentences of classical and vulgar bourgeois economy and to confront the by Marx established 'laws' with a them supposedly contradicting 'reality'.

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Varga in his treatment of the problem of 'gold inflation' *apparently* wants to unite two different 'monetary theories' with each other. On the one hand the 'metal theory of money', by which he understands 'the conception, that the value of money is determined in the same way as the value of any commodity, is equal to the value of gold, which the money unit really contains, resp. represents as paper money', – on the other hand the from the paper money

circulation derived law, according to which 'the total amount of circulating money does not represent more value, than that small amount, which would suffice for the transaction of circulation'. In reality however he does not at all recognise that which he discretely calls 'the metal theory of money', by which he in reality however means nothing else than *the Marxist theory of the commodity character of money*, and is entirely like once Ricardo (only of course 'vulgarly' and not 'classically') 'dominated by the phenomenon of value tokens depreciating because of their quantity'.[287] The validity of the 'metal theory of money' depends in his opinion on the 'presupposition', that 'every amount of gold inside the capitalist economy can function as money, as general equivalent, as world money'. It no longer holds when in a country a situation occurs in which 'no further amount of gold as money material – neither as means of circulation, nor as means of payment – can find employment'. This whole presentation of Varga obtains however a real sense first then when one supplements the by Varga *expressed* 'presupposition' for the recognition of the 'metal' monetary theory, with the much more broader presupposition, which is *silently* made by Varga in his whole presentation, and which consists therein that *all the 'on the territory' of a country existing gold* (perhaps with exception of the industrially processed and for luxury used gold – but even this assumption Varga does not make explicit) *also actually is employed as means of circulation (and payment)*. That is to say thus, that the 'metal theory of money' for Varga from the start holds only under a presupposition that in reality only for paper money (which only is employable as means of circulation and payment) appertains regularly, by contrast for gold at most in an exceptional case. Varga, who wants to transmit a from the observation of paper money circulation derived concept to gold money ('gold inflation'), spares himself the trouble of a substantiation of this procedure thereby that he from the start silently makes an in reality invalid presupposition, which already secretly removes the first to be proved similarity of paper money and gold circulation.

Very clearly this erroneous circle becomes evident already in the way that Varga presents the *emergence* of the by him examined 'gold inflation'. He asks, what would happen, 'when circulation already entirely can be transacted by gold money' and then 'still further gold accrues'. Apparently for him it is entirely self-evident, that this to the 'circulation' 'accruing' gold can come only from abroad and that conversely all the gold present inside the country already is found 'in circulation'. That is to say thus, he presupposes, that in his up to the 'inflation'-point gold-soaked country on the one hand circulation is completely transacted by gold money, on the other all existing gold also revolves in circulation. He takes thus,

[287]Marx 1987, p. 405.

although he *talks* a bit of 'general equivalent' and 'world money', in reality no account of the other by gold money, besides the circulation function, at any time fulfilled functions, which paper money cannot fulfil. And he does not understand (in his capacity as economic 'theorist') above all the special, of entirely different kind functions, which the real (gold) money *in international 'traffic'* at any time, and particularly in such a critical situation as today has to fulfil. The by him silently accomplished equation of the in one country *existing* and the in one country *for the internal and world market circulation actually employed* money forgets firstly the fact that every country of developed bourgeois production always has to concentrate in its bank vaults massive treasures as a *reserve fund* both for its internal circulation as well as for world market circulation. It overlooks secondly (what the economist Varga very well recognises in another form), that the real (gold) money as world money functions not only as measure of value, general means of payments, general means of purchase, but moreover also in its capacity as '*absolute social materialisation of wealth*' has to fulfil certain important and necessary functions.[288] Only because Varga without further ado equates the factually existing gold in a country with the circulating gold in a country, and therefore that the total 'money' from the start in truth assumes the only for the 'money-tokens' valid law, can the point indicated by him as beginning of 'gold inflation' ('where internal circulation entirely is transacted by gold money, respectively gold certificates with hundred per cent gold backing' and then still further gold accrues from abroad!) obtain the significance of such a decisive turning point, as it with him factually obtains.

Still more distinctly the erroneous circle becomes evident in his further statements about the *concrete forms*, in which according to his opinion the 'gold inflation' in the United States soon has to appear. For the further development of the money relations after the occurrence of the critical point there are for him 'two possibilities'. Either also the new 'accruing' gold is still 'forcefully pressed into circulation' (? K. K.). In this case takes place following the old, by Marx[289] refuted claim of Ricardo, oh pardon, following the new, from a detailed study of contemporary empirical phenomena of American-European 'economic life' derived discovery of Varga, what would occur with a corresponding increase of paper money value-tokens. The real or in certificate circulating gold coins become 'depreciated tokens of themselves' (Marx). Varga literally says and undoubtedly with a certain delight: 'There come into play for gold the laws of pure paper money circulation'. (And he continues, still more

[288]Marx: 'wherever it is not a matter of buying or paying, but of transferring wealth from one country to another, and whenever its transfer in the form of commodities is ruled out, either by the conjuncture of the market, or by the purpose of the transfer itself; for instance subsidies, money loans for carrying on wars or for enabling banks to resume cash payments, etc.'. Marx 1976, p. 243 and footnote 61.

[289]Marx 1987, pp. 402 and following; 1981, pp. 680 and following.

delighted, on this basis to charge against the Marxist 'law of value', a charge with which we will occupy ourselves first later).

While however this first form of gold inflation according to Varga's further statements would occur anyway only within the national frame and would be cancelled internationally by a from it drawn 'balancing tendency' of the 'capitalist mechanism' by way of a 'repulsion of excess gold', the matter stands differently with the second, alternatively with the first as possible by Varga designated case. This case consists therein that the 'free coinage of gold dollars is suspended and now 'the gold coins obtain an agio compared to bullion'. Then according to the economic theory of Varga 'the excess bullion' indeed would 'immediately flow out' (? K. K.), like in the first case the total excess gold was 'repulsed' (? K. K.) by the 'capitalist mechanism' itself, but the 'gold inflation' would now, as inflation of the total gold in the world compared to the minted American dollar coins, also internationally come to light. 'The dollar would lose the correlation with gold, its value no longer bound to gold, but internationally overvalued, and its valuation would fluctuate similarly to any of the non-backed paper moneys, but above the nominal original gold value'. (Why in this case the dollar coins are at all still constructed as gold, remains the secret of Varga!)

One sees, Varga has established his 'gold inflation' *in both cases* thereby, that he has transformed *gold (from paper) into paper*. In the first case all (coined and uncoined) gold becomes in the same way inflated and by inflation devalued paper money, though only in one country and only temporarily. In the second case the uncoined bullion becomes inflated, just as in the first case all gold. By contrast in this case the coined gold transforms itself compared to the bullion–papermoney into overvalued dollarcoin–papermoney and gets this overvaluation also internationally and lastingly. All this explains itself also quite simply. For when gold takes on the characteristics of paper money, it is subject naturally also to the 'laws of paper money circulation', and in particular its 'value' is determined no longer after the value of the golden substance which it contains. The paper *gold* becomes undervalued (it realises in exchange against commodities no longer the value contained in it). The paper *gold coins* are shielded from this devaluation; they therefore become overvalued (first compared to the inflationary paper gold, later – after the 'balancing of the international price level' – in lesser degree compared to gold and all other commodities).

So far the fable of the 'money theorist' Varga swarming in the merry realm of fantasy. Let us now move to the objections, which can be raised against this hallucination from *the standpoint of Marxist critique*.

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Firstly it should be pointed out that from the standpoint of Marxist theory, which considers real (gold) money as a commodity, and as the real, in this context to be answered question asks the question about the relation between the value of this real money and the value of other commodities, there exists not any difference between the both by Varga differentiated phenomenal forms of his so-called gold inflation. Gold is devalued in relation to the other commodities in both cases in the same way, and in both cases this effect takes place first nationally in one country, to then become internationally balanced through the by Varga (unproved) assumed 'balancing tendency'. Also in Varga's second case, since by the suspension of free dollar coinage *ex hypothesi* is prevented only a devaluation of the dollar coins, the value relation between gold coins and commodities thus will not be changed, the apparent agio of gold coins compared to bullion signifies in reality a price increase of all commodities, measured by the real measure of value, by gold – and hence [signifies] a devaluation of this real money, a devaluation of gold compared to all other commodities. And again similarly to the first case, also in Varga's second case the devaluation of gold compared to the other commodities in a country of gold inflation takes place only temporarily. In both cases the by the economic 'theorist' Varga assumed 'balancing tendency' [the 'repulsion of excess (coined and uncoined) gold', resp. the 'immediate outflow of excess (uncoined) gold'], *if it takes place in reality* (!), eventually leads again to a unitary international value relation between gold (the real world money) and the other commodities. A real devaluation of gold thus would under the by Varga assumed (by us not yet examined) presupposition in both cases take place only temporarily, in order to be internationally at once automatically balanced.

Our second critical objection is aimed against the peculiar 'balancing tendency', which in the assumption of the economic 'theorist' Varga in both by him differentiated cases of 'gold inflation' would be accomplished through the 'capitalist mechanism' itself. Here most clearly the by us in the beginning of our analysis highlighted antagonism is shown between both souls in Varga's breast, the economic reporter soul and the economic theorist soul. And here is shown most clearly also that the 'bizarre idea' about the relation between the disturbances in the circulation sphere and in the total economic sphere, which we further above detected in the theorist Varga, really is no accidental lapse, but correctly denotes his 'theoretical' basic conception. The question is namely: How does the economic theorist Varga actually arrive at the presupposition that in the cases of American 'gold inflation' described by him those mysterious events will occur, which he in one (the second) case designates only quite briefly as an 'immediate outflow of excess bullion', which he however previously with the

description of the other (the first) case had more closely described with completely unambiguous clarity and exhaustiveness? This through the 'mechanism of capitalism' 'accomplished' 'balancing tendency' consists accordingly therein, that in case of 'gold inflation' due to the by gold devaluation in the United States occurring relative rise of the price level of all commodities 'it would prove to be advantageous, to import commodities from abroad against gold payment, hence a passive balance of trade, repulsion of excess gold (respectively immediate outflow of excess bullion) to abroad until the balancing of the international price level' (p. 1884).

The economic 'theorist' Varga appears here so captivated by a *blind trust in the harmonious self-regulation of capitalist production*, as the sober economic statistician and historian Varga would not have dared to permit him. The economic historian Varga has told us that the production of the United States in the last ten years has grown so 'enormously', that precisely thereby a giant surplus export (20 billion dollar in ten years) has become necessary and precisely hereby that 'gold flow' turned into a torrent, which since a long time daily washes no less than one million dollar of gold on the American shores. When now until the moment of complete gold filling of all channels of American circulation continually this 'gold flow' has flowed across to America, why then shall this 'flow' suddenly turn around its current, instead of American surplus export take place a surplus import, a 'passive balance of trade' and as a result the 'excess' gold again as 'immediately' flow out, as it apparently beforehand also flowed in? And all this due to the sole reason, because a 'gold inflation', that is thus a disturbance of the 'money circulation', a certain 'manipulation of the circulation medium' has taken place? This one assumption of Varga shows clearly that the whole Marxist refutation of the Ricardian error passed by the Marxist 'theorist' Varga without a trace. Like in Ricardo (who as bourgeois economist still with a certain right could ask for the mutual 'correlations' without causal significance, rather than for the real ground and real consequence, the cause and effect), so also with our economic 'theorist' the real cause and effect has been mystically reversed. Entirely like Varga today makes the American export and import dependent on the 'gold inflation', entirely similarly thought more than a hundred years ago David Ricardo, that with a failed harvest in England gold is exported not 'because corn is needed and gold constitutes money, i.e., it is always an efficacious means of purchase and means of payment on the world market, but because the value of gold has fallen in relation to other commodities' and hence the currency of the country suffering from crop failure is by a kind of inflation ('the existing quantity of money in circulation exceeds its

normal level') devalued.[290] This theory of the great bourgeois classic and his epigones has been however meanwhile practically (by the fiasco of the by Ricardian ideas dominated bank legislation) and theoretically refuted in England itself and finally crushed by the critique of Marx, – in order to celebrate today a happy resurrection in the 'theoretically interesting' remarks of Varga. So strongly is Varga as economic 'theorist' captivated in superseded dogmas of bourgeois economy, that he in his capacity as theorist forgets everything which he is in his other character mask reports himself. He has told us that the eb in the 'gold flow' in September was a 'phenomenon caused by the great foreign loans'. And he has in his 'economic' observation quite rightly stressed, that these September and all previous and later American foreign loans and capital exports, and likewise also the giant gold import itself, came into being only because American production has a strong and ever growing overproduction of commodities and the United States consequently has and must have an ever growing surplus export. He has as 'economist' shown us also the direction, in which this development process in a persisting capitalist economic order can only develop further. He has in the third part of his article and in the following article ('The United States as capital market') treated the increased capital export (wherewith he however at the end, p. 1885 above, once more falls back into his 'money-theory' qualm!). This himself progressive economist sticks on the as economic 'theorist' backward one and the mystic representations of the classic bourgeois economy and their bourgeois epigones and portends that in a country, which experiences the events designated as 'gold inflation', *due to these events* the balance of trade again will become passive (p. 1884). The consequence, which with consistent thinking from this results (and for the bourgeois theorists of the eternal 'circuit' also not at all would have anything absurd), is that the same 'capitalist mechanism', which laid the 'gold flow' towards America and next, after the occurrence of 'gold inflation', again has laid it away from it, will transform back the concerned country at the end also again from a commodity and capital exporting imperialist country into a not only commodities, but also capital importing colonial country, – whereupon then the same process from the start can begin again, in circles around, whether towards or away from, like with the prototype of all these derived representations, the rising and falling of commodity prices on the capitalist commodity market.

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Of such nature are the 'theoretical' reflections on the 'problem of gold inflation', on which Varga seeks to support his attack on a few main theorems of Marxism. Insofar as this attack

[290]See Marx 1987, pp. 407–8 and both the there literally mentioned places from a money-theoretical writing of Ricardo.

is specifically directed against the Marxist teaching of the commodity character of money, we have already established its fundamental falsity. There still remains the settlement of the directly against 'the law of value' aimed partial attack, – and finally a positive reference to the real Marxist resolution of the contradictory phenomena, which are treated by Varga in false form under the concept and name of the so-called 'gold inflation'.

His *direct attack on 'the law of value'* Varga connects with the description of the first of both, for him possible, phenomenal forms of gold inflation. We have already seen that between both Vargaian phenomenal forms of Vargaian 'gold inflation' there does not exist a fundamental difference at all. If thus in the first case (as Varga claims) reality would contradict the law of value, then it would also in the second case.

In truth however both, by Varga envisioned contradictory phenomenal forms of so-called gold inflation, even if they were to occur in reality, would neither the one nor the other say something against the validity of the Marxist 'law of value'. Varga denotes, after he in the above already explained way with his from the law of paper money circulation derived 'quantity theory' established the possibility of an 'inflation' of gold in the United States, with the greatest satisfaction the following 'paradoxical' consequences:

> There would thus occur the paradoxical situation, that full-valued gold dollars in the United States would be undervalued, that is their exchange relation against other commodities would not proceed according to the law of value. With the exchange of gold dollars against commodities a greater amount of labour time, that is value would have to be given, than is contained in the exchanged commodities.

This whole exposition of the economic 'theorist' Varga rests on a very 'vulgar', but admittedly until now not only with bourgeois economists, but also with the 'Marxists' still very widespread misunderstanding of the *real meaning of the Marxist law of value and the total Marxist critique of the by him encountered bourgeois political economy*. Everyone knows, that the law of value of Marx (insofar entirely like with the law of value of *Smith* and *Ricardo*!) determines the exchange value of commodities according to the socially necessary labour time for their production. When it transpires that the real exchange relations somewhere 'contradict' this law of value, then this is for the law of value of classical bourgeois economy to a high degree fatal. And Ricardo notoriously goes to any lengths, to explain away all these 'contradictions' or to situate them still as possible as meaningless and void: eventually he contents himself that his law with certain, specifically determined and limited exceptions and modifications is valid. It is entirely *different* with the validity of the

Marxist law of value. This law wants as a social law of nature [*gesellschaftliches Naturgesetz*] of the capitalist economy definitely not only 'to apply' in the sense, that its validity would depend, on the fact that the exchange of commodities really happens 'according to their value, or approximately to their value'. This occurs according to Marx at all only on a relatively 'low' [*niedrigen*] and historically 'early' [*frühen*] stage of development of capitalist production.[291] And also regardless of the fact that the Marxist law of value quantitatively determines the exchange relations of capitalist economy also there, where superficially viewed, commodities do *not* exchange at their values, it is also still in a deeper sense a deadwrong conception of the real meaning of the 'validity' of the Marxist law of value, when one believes that this law as a 'general law' of the epoch of capitalist commodity production has validity only for as long and insofar, as the for the continuous progress and further development of this capitalist commodity production necessary exchange-acts come into existence really in general and everywhere, in the through the law of value directly or indirectly determined quantitative relations. The *Marxist* law of value holds much more in a 'paradoxical' way also then when the exchange-acts in the through the law of value determined relation do *not* come into existence and precisely thereby a disturbance of the normal progress of capitalist production (a crisis), an inhibition of its further development, and finally its shock and decay is called forth. Yes, the 'law of value' obtains precisely in this second case, understood in Marxist–dialectically–revolutionary fashion, first its full and real, social historical reality.

Varga, who from this dialectical revolutionary main sense of the Marxist 'Critique of political economy' and all its laws knows nothing, and in this way of the bourgeois economists asks *only* for the laws of the persisting capitalist economy, not *simultaneously* for those of its revolutionary overthrow and its historical transition in a new, by other laws determined economic form, is from his standpoint with his attacks on the Marxist law of value, on the Marxist teaching of the commodity character of money etc. entirely as correct, as once Eduard Bernstein with his revision of the dialectical and revolutionary Marxism had been correct. But Varga is entirely as previously Bernstein wrong, when he believes that with his representations on the validness or invalidness of these by Marx recognised 'laws' of the classical, bourgeois economy to have struck the real meaning of the validity of these laws in the system of the Marxist *critique of political economy*. If Bernstein and Varga with their representation of the meaning of the law of value were correct, then at the latest the 'final crisis' and the eventual downfall of the capitalist economic order, that is thus the

[291]Marx 1981, p. 277.

revolutionary transfiguration of this capitalist economic order in a period of proletarian dictatorship would have to furnish the conclusive proof, that the 'law of value' in the real reality in the end factually does *not apply*. In truth however of course precisely in this period the Marxist dictum is fulfilled in its deepest and most general sense, that, like all other 'social laws of nature' of the historical epoch of capitalist commodity production, so also the law of exchange value 'asserts itself only in its antithesis'.[292]

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From our critical analysis of the 'theoretical' remarks of Varga on 'the problem of gold inflation in the United States' ensues concurrently the *positive critical resolution* [*Auflösung*] of this pseudo-problem. In all phenomena of this so-called 'gold inflation' (that is, the under determined conditions within very narrow limits thinkable occurring of a temporary apparent relative devaluation of gold compared to other commodities in the United States) there would, if they in reality would occur, invertedly [*verkehrt*] be reflected always a mere relative price increase of commodities in America. In reality however for the occurrence of such phenomena there exists not the least probability. They will occur today in America as little, as they in the time in England took place, when Ricardo fantasised [*zurechtphantasierte*] them *for the purpose of* his false theory.[293] And all the 'contradictions' of the phenomena observed presently in America in the circulation sphere appear unriddled, as soon as one assumes that with them it is not essentially about events in *money circulation*, but reversely about events in *commodity production*.

Varga could have quite considerably disburdened and for the most part entirely spared his 'interesting' musings on the phenomenon of the American 'gold inflation' and the thereby raised 'entirely new problems' (p. 1885 above). Marx has already in the first part of the first volume of *Capital* given a perfectly adequate key for the solution of all riddles of contemporary American 'gold inflation'. The last sentence of this part reads: 'Whenever these hoards (of banks) are strikingly above their average level, this is, with some exceptions, an indication of stagnation in the circulation of commodities, i.e. of an interruption in the flow of their metamorphoses'.[294] That is to say thus: The fact that in America gold is 'excessively' amassed, shows that the American producers by the exchange of their exported commodities against foreign gold from the complete, of two metamorphoses consisting, capitalist commodity exchange act C–M–C, have first executed the one half, and that the

[292]Marx 1987 p. 302.
[293]See Marx 1987, pp. 407 and following, pp. 415 and following.
[294]Marx 1976, p. 244, similarly Marx 1987, p. 383 'The result of an interruption in the interchange of products and therefore commodities congealed in their first metamorphosis,' – as 'gold-chrysalis'.

entire process of international social interchange here is congealed and interrupted. The American commodity producers, who sold their commodities not to an itself commodity producing and selling capitalist producer abroad, but have obtained for their commodities only from a foreign gold owner gold as 'absolute social materialisation of wealth', have not yet truly realised the value contained in their exported commodities for the transferred product. The excess 'gold' in their hands represents only the changed form of the commodities produced and exported by them. The inability to sell these commodities (the capitalist overproduction of the United States) appears in the phenomenon of the excess 'dead stock' of gold and the thereby repercussive under circumstance perhaps (!) conditioned new (secondary) stagnation and disturbances in the circulation and production process. Therein consists the entire 'theoretical' disclosure of the mysterious problem of the so-called American 'gold inflation'. The contemporary and artificial difficulties of American business people and 'economists' spring not from a 'gold inflation', but the overproduction of the American capitalist economy. Only the economic 'theorist' Varga fantasises that the difficulties can be overcome by the automatic *'balance tendency' of the 'capitalist mechanism'* itself. The 'economist' Varga shows us the real path on which the *American capitalists and imperialists* strive to actively [*handelnd*] free themselves from their real 'worries', springing from capitalist overproduction of the American economy. And the Marxist law of value and the entire Marxist critique of bourgeois economy have their significance therein that they show the *proletariat* the path, how it can exploit these growing difficulties of the capitalist production, to transcend in a revolutionary struggle this capitalist economy with all its 'social laws of nature' resting on the unconsciousness and planlessness of this class economy.

What shall we say thus in conclusion about the 'theoretically interesting' remarks of Varga on the problem of gold inflation? Marx noted about Proudhon: 'Nothing is more tedious and dull than the fantasies of *locus communis*'.

Chapter Seventeen

The Value of Gold and the Purchasing Power of Money[295] (1927)

Aleksandr Finn-Enotaevsky

Aba Joelevich Finn (1872–1943) was born in Kovno (Kaunas), in present-day Lithuania, to a Jewish family. He was active in the Russian Social Democratic movement since the early 1890s. He studied at the gymnasium in Nikolaev, then entered the Physics and Mathematics Faculty of the Imperial University of St. Vladimir in Kiev, where he majored in chemistry. In 1896 he was arrested at Medical Faculty in Moscow and expelled to Enotaevsk, in the Astrakhan Oblast, a place from which he took his pseudonym Enotaevsky. After serving a prison sentence and again being exiled, he moved abroad, to Germany, Switzerland and France, where he studied law and economics. He wrote his first articles on economic crises in 1901 and 1902. A. Y. Finn-Yenotayevsky is mentioned in several letters by Lenin; in one of them, dated 19 November 1901, he suggested to Plkehanov that Finn's article "The Present Industrial Crisis" could "go into *Zarya* No. 4." Upon his return to Russia, Finn published articles on economic and financial matters in various journals and engaged in editorial work. The results of his research were summed up in his main work, *The Modern Economy of Russia 1890-1910* (1911), which was published in the revised 1925 edition with the title *Capitalism in Russia, 1890-1917*. From 1913 to February 1917 Finn worked in St. Petersburg as a statistician in *Togrovo-promyschlennij Bank*. From autumn 1917 to summer 1918 he published in the opposition newspaper *Novaya Zhizn*. After the Bolshevik revolution, Finn taught political economy at the Leningrad Polytechnic institute from 1924 to 1930. In the spring of 1930 he became head of the Faculty of Political Economy's Department of Money and Credit. He was arrested in late 1930 and sentenced at the 1931 Menshevik trial (biographical data taken from Dmitriev 2012).

During the 1920s Finn published a series of articles on money in the journal *Sotsialisticheskoe khozjajstvo* (*Socialist Economy*), including the present one. It refers briefly to the pre-WWI debate, stressing that Kautsky was right to reject the

[295]Theses of a lecture of professor Finn-Enotaevsky, read at a joint meeting of the Institute of Economic Studies and the Institute of Conjuncture of the N.K.F. [People's Commissariat for Finance] USSR 25 February 1927. Printed with permission of the author. Ed. [Finn-Enotaevsky (1872–1943) was active in the Russian social democratic movement since the early 1890s. On Finn's analysis of postwar gold value, there was a reply in 1928 by Soldatov (1888–1963).]

idea that the value of gold is determined by the least productive mine, though *en passant* remarking that the cyanidation process in the pre-war period 'touched little, or not at all, in the opinion of many, the value of gold'. Finn's analysis of the postwar gold value received a reply in 1928 from Soldatov (1888–1963). Finn intended to write more in depth on money (and credit), particularly gold, but did not come around to doing it.

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1. The common claim (see Cassel, Keynes, Hawtrey, Fisher, Lehfeldt, Herman[296] and others), that the value of gold, and consequently also gold money, in comparison with the pre-war time, fell by approximately one-third, is wrong: there was a fall only of the *purchasing power* of gold money corresponding to the rise of the world general price level, on average for the most important countries by fifty per cent.
2. The value of money and its purchasing power are different concepts. The first is determined by the value of the *commodity* gold, represented by it, which from its side, is determined by an *internal* measure – social labour time. Purchasing power, applying *only to money*, *is relative*, a function of two elements: the value of money and the value of commodities. The value of money is not an abstraction, but a *concrete actuality*. Money is the pure expression of value. An evident illustration: the banking world operates with money and money capital, as *values*. In contrast, the purchasing power of money or, what is the same, the relative value of money in comparison to all commodities (and services), being expressed incompletely and inaccurately in the most perfect indices, is only an abstraction, a statistical average.
3. Gold as *commodity* has only a value; it has no price. Commodities have value and price. The reciprocal of the purchasing power of money – the *price* of a commodity is likewise a function of *two* variables: the value of gold and the value of the commodity. The value of gold is not a reciprocal of the price level.
4. The social, instinctive in the course of history, selection of the commodity gold from the whole mass of commodities and the vesting of its function of measure of value, of general equivalent, of money was dictated by the iron necessity to resolve the contradiction of the commodity world, by force of the separation of exchange value from use value. Removing this contradiction into this one, general, exclusive commodity, the commodity world has

[296][It is not clear who the economist named Herman is.]

gained the necessary to it *form* of movement. So long as the commodity world exists, gold, as basis of the money and credit systems, is indispensable; the existence of social wealth, *money*, as a *thing*, *beyond* all the rest of the *commodity* world is inevitable. In this lies the heart of the matter: with purchasing power of money this is erased, these social contradictions are hidden. *Credit, the second* social form of wealth, replaces money, it facilitates the realisability of commodities, but does not eliminate the necessary existence in the world of commodities of the *primary*, basic form of social wealth, money, in the form of a *real thing* – gold.

5. Gold, as general world money, and not by force of its quality, as *commodity*, and not by force of its special *natural* qualities as product, gold as *general world* commodity, differs from *all other commodities* in its *exclusive realisability*, [in] its *special* ability of *direct* exchange for *all* commodities, [that] resolves the contradiction, arisen from the different *national* values, from the different purchasing powers of the money of different countries. *Genuine* money is always *world* money, gold. The unobstructed exchange of gold for national currencies provides gold *everywhere* [with a] purchasing power of the given countries without difference of their money and credit systems.

6. Gold in normal conditions has everywhere one and the same value (abstracting from transport, insurance and so on). But by virtue of the operation of the *law of value* in the world – international – sphere [being] *dissimilar*, than in the national sphere, gold obtains (costs) differently for different countries, in dependence on the differences of their national measure of value, determined by the differences of their social labour time, that depends in its turn on the level of their economic and general social development.

7. The purchasing power of money in different countries is necessarily different. And this, both owing to the difference of economic, social and natural conditions of production and consumption of the given products, and also owing to the difference of national measures of value. An illustration of this is the difference of national wages. Under the same value gold everywhere as money therefore in some countries is always more expensive, in others – cheaper. In America, for example, also before the war it was cheaper than in England, [and in] the latter it was cheaper than in Germany...

8. The value of gold, like also every commodity, is determined by the internal measure – by labour time, [and] externally manifests its magnitude in an *amount* of other commodities, in relation to their values. In developed commodity exchange, and all the more in capitalist exchange, where commodities are sold at prices of production, the magnitude of the value of money and the prices of commodities are given *historically*. We can observe only the *change*

of their magnitudes. These changes of the value of money and commodities are manifested in the changes of commodity prices. Already Ricardo stated the position: if we observe that an ounce of gold is exchanged for a bigger amount of the same commodities than before, and with this it turns out that the given amount of gold is obtained, due to change in natural conditions and improvement of technology, with a lesser cost of production, than one can draw the conclusion that the cause is on the side of money.[297] *Analysis* of the indices, but not the indices themselves, *analysis* of commodity prices, wages, rents, *analysis* of the phase of the industrial cycle, *analysis* of the situation of credit and money in the world economy, [and] from the other side, analysis of the conditions of world gold mining, and for a *long* period, as the different factors do not at once have an impact – solves in the final instance the problem.

9. The theoretical analysis of the turnover of money capital, invested in gold production, shows, that, having been turned in fixed capital, in constant circulating capital and variable capital, it (fixed capital) produces a product, the money sum of which is equal to variable capital, expended on wages, plus constant circulating capital, expended on means of production, plus part of the value of absorbed fixed capital, plus profit, rent and other parts of the produced surplus value. If the sum of obtained money from the product is less than the enumerated costs, and the value of gold with this did not change, then the particular mine, having become unprofitable, closes. If the unprofitableness affects the whole industry and protractedly, then the reduction of mining leads to a change of the value of gold, which is expressed in the fall of prices of commodities, and with that in the fall in future sums of money, necessary for conducting production. A study of the Transvaal industry, [which is] placed on strong capitalist legs, shows *in practice*, that all calculations of the costs of gold production are carried out in data of gold.[298] The capitalists reckon with costs of production, more precisely with prices of production, expressed in money, in their relation to gold, and with the value of the product, expressed in gold. This is not denied also by Fisher.[299] He considers, however, that it is 'more convenient' to express both the product and the costs not in gold, but in data of commodities, in the purchasing power of gold, which, in his opinion, is one and the same. This is also untrue: in one case a concrete measure of value is a single, exclusive, commodity – gold, the value of which, by force of special conditions of mining and sale of this commodity, remains generally stable not only in the course of annual turnover of capital, but also cyclically, in the other case an abstract measure – an index of prices of

[297][See Ricardo 1821, p. 10.]
[298][No reference given.]
[299]Fisher 1911, p. 101.

commodities, the value of which moves quicker, differently from one and other and from the value of gold. Living *practice* not only of capitalists – money, industrial, commercial capitalists – showed, that the most convenient and accurate within various calculations of production and trade proceed from money – gold, as stable value, and [that] the change of prices of commodities is accounted by the latter, but also that wide layers [of the population] are accustomed to measure their income – this relates also to the struggle for real wages – and credit relations in data of metallic gold money. And this for *short*, even cyclical, periods theoretically is more correct [than] various 'scientifically' laboured 'regulated' moneys. Of course, we here talk about *normal* – gold – moneys, and not inflated moneys, where a fall of the value of the 'paper' standard [sic] of *sick* money occurs much quicker [than] the value of commodities. And, of course, we here do not forget, that the *value of gold*, and all the more the purchasing power of gold money, is *variable* over time.

10. The theory of Fisher, starting from the purchasing power of money and the marginal costs of production, arrives at the conclusion that the mining of gold depends on the purchasing power of money, or, in other words, on the general price level. According to this theory the mining of gold should have to fall in phases of upsurge and flowering of industrial cycles, when prices increase and when demand also for gold increases. Although prices, having an influence on costs of productions, can have an influence on the mining of gold, Fisher's conclusion is not confirmed by reality, which refutes it and his fixed price of gold. The evidence of gold mining shows, that it grows also in times of high prices and falls also in times of low prices; it is enough to compare the 1870s and 1880s with the 1890s and 1900s. Cassel, rejecting the theory of marginal costs of Fisher, rejects at once also the theory of costs in general, but, being himself a theorist of the purchasing power of money, a quantity theorist, presents the [following] position; 'the influence of gold production upon the general price-level depends on the quantity of gold which can be produced at the prevailing price-level, not on the "cost of production," which is an entirely vague concept'.[300] This position in essence repeats Fisher, that gold mining depends on the price level, that is on the existing purchasing power of gold. It, further, observes a by no one disputed fact, that gold influences prices by its quantity. The first position, that the quantity of extracted gold depends on the price level, as we already showed, does not always correspond to reality. A diminution of the costs of production, depending on technical and natural conditions, often leads to no real action on prices. Moreover, also in these branches speculative investment of capital occurs in times of phases of boom. And, finally, there takes place a change of the price level, *from the*

[300][Cassel 1932, p. 480.]

change of the value of gold. This is what operates – a series of factors, and – counter-posing factors. The second position – the influence of the quantity of extracted [gold] on prices – is a fact, on whose explanation also political economy breaks its head until this day. Cassel again here remains on the surface.

11. The theory (shared also by some Marxists: Hilferding, Otto Bauer, Varga), that the value of gold is determined always by the cost of production at worst conditions is wrong. The facts show the contrary (Taussig, Kautsky).[301] They confirm the correctness of the theory of Adam Smith–Marx, according to which there exists competition also *inside* this branch, and in dependence on conditions of production and sales [realisation] there dominates the best, worst or average companies. With this should not be left out of sight, that the competitive ability of one or other company, the opening or closing of them, depends not only on the prevailing *value* of gold on the world market, but also on the situation of *costs of production*. The theory of Marx leads to the conclusion that neither the 'fixed price' of gold nor the commodity price-level determines the quantity of extracted gold and the situation of gold producers. A fixed price – this is always a fiction, but the price-level has an influence usually *on individual* mines. But if the height of prices reverberates onto all gold producers, heavily increasing the costs of production, so that it becomes unprofitable, then there happens an entirely different phenomenon: not the mining depends on the price-level, but the price-level changes from the changed conditions of gold mining. The changed costs of gold production, having become a general dominating phenomenon, changes the value of gold, the value of money, and therewith also the prices of commodities. Against Cassel, this happens precisely on the basis of changed costs of production. Against Fisher, this happens on the basis of the changed value of gold, although all gold in coin remains without change, that is under a constant standard, which is its *ceiling price*.

12. Gold acts in simple as well as in capitalist commodity production and trade, by its *value and quantity*, in which connection also the change of its value is manifested in quantity, but the action is different. The change of the value of gold impacts first of all on the world market, it acts on the exported commodities, calls forth a differentiation of price of commodities of different branches and, transmitted later to all wages, increases in branches, with higher prices, the profit. This happens until when prices do not equalise and wages do not rise. The change of the value of gold stimulates, in this way, the demand on commodities of best and most productive consumption, gives an impetus to the development of production and, since this is connected generally also with an increase of production, then also under a termination

[301][The reference is likely Taussig 1911, pp. 262–3.]

of the fall of the value of gold, the eventual decreasing of the value of constant capital, if this covers the big branches and for a sufficiently long time, raises the general rate of profit. This is the theory of Hume–Marx. There exists, however, a deep difference between the devaluation of money called forth by inflation of paper money, and the fall of the value of gold, though on first view between them there is similarity. In the first case a manipulated industrial cycle is created.

13. If there takes place an increase of the quantity of gold without change of value, then the influence of this quantity is expressed in an increase of the *income of the given countries*, and with it the consumption demand, and its *capital* in money form, invested for productive purposes, which expands the national, and later also the international market (we abstract now from credit). Here there takes place an increase of general demand by force of an increase of commodity production in a particular form – gold. Question: is this increase of production of gold producers *always* connected with general demand? Answer – no: the increase of extracted gold can lie without movement, as treasure, as latent capital. The transformation of it into active money depends not on its quantity.

14. Demand for gold grows together with the development of the money and credit economy, in connection with the very conditions of capitalist production. But the operation of demand for gold, as for a particular commodity, is different than that for ordinary commodities. This does not mean that demand has no influence on the value of gold. Leaving aside local and temporary fluctuations of the value of gold by demand, the action of world demand for gold is expressed more on the quantity of mined gold, than on the value, and influences the latter only in the long period. From the other side, the *supply* of gold, by force of the special function of this commodity, is peculiarly manifested. *Annual* gold extraction, represents an insignificant percentage in comparison with the existing reserves of it in the world economy, does not define the value of the latter, but on the contrary, it finds the value of gold on the world market given, as also the commodity prices, measured by this golden measure. There is necessary an exceptional, in force and length, condition of supply and demand, for the world value of gold to have undergone a change. All this makes the value of gold *stable*. And the change of the value of gold, appearing as the result of a *long and deep change in the costs of production*, in dependence on significant change of the *natural and technical conditions of mining* of it, marks an epoch in the history of money and world economic life. Such epochs were the end of the sixteenth and seventeenth centuries, in connection with the opening of American treasures and mines, in the 50s and 60s of the nineteenth century in connection with the Californian and Australian deposits. The opening of the Transvaal mines at the end

of the 1880s and the new chemical method (cyanidation) of processing mines in the 1890s manifested, in the main way, in an increase of the *quantity* of mined gold, touched little or not at all, in the opinion of many, the value of gold. And this, on one side, due to the increase of world demand for gold, and on the other – the peculiarity of gold production, in which a reduction of cost of production due to improvement of technology leads often to speculative expansion of mining in the worst mines and to an often unjustified expenditure of labour and capital. Finally, after the last decade extraction of gold takes ever more a *regular* character by way of a systematic development of *deep deposits*, which demands a *big* expenditure. This is observed both in the United States and specially in the Transvaal mines, which give now half of world extraction, regardless of the comparatively insignificant percentage of gold, which however is located more or less equally in mines.

15. A depreciation [*obestsenenija*: impairment] of gold in the war and postwar time there could not be. There was no *demonetisation* of gold. The role of gold as *measure of value* remained unshakable everywhere: also in countries with a *variable*, paper, *standard* [sic]. The inflation of paper money did not depreciate gold, on the contrary, all over where inflation was stronger, there the value of gold stood higher, for example: Germany, Russia. The reduction of the function of gold, as means of circulation, was compensated by its role as a means of *cash*, which everywhere increased (As illustration can serve the movement of gold reserves in the central issuing institutions of the belligerent and neutral countries). The role of gold, as *means of exchange in international* trade, as means of purchase and payment, rose by force of the weakening of credit and the disorder of the credit system (As illustration can serve the movement of gold in the United States and England during and after the war). The reduction of coinage of gold does not at all show the depreciation of gold, earlier too there was also no necessary connection between mining and coinage. The increased demand for *silver* and the strong rise of the price for it during the war and in the first years after it is explained precisely by the demand of world trade in precious metals. The *saving* of gold also prompted [people] to operate more with silver. This is illustrated also by the fact that world coinage of silver grew strongly with the goal of meeting internal demand for the metal, and later – with the withdrawal of also silver from circulation – also the remelting of silver in connection with the rise of prices for silver and demand for it for payment of the East. The prohibition of export, the obstruction in the transport of gold, as an instrument of conducting war, the suspension of free coinage of it, the rise in price of transport and insurance – prevented an equation of the value of gold in different countries, and the difference of the value of gold in individual countries grew; the distance between gold points

increased. But this, like also the exceptional measures, artificial decrease of the value of gold, whether in the British Empire, or the Scandinavian countries during the war, or in Russia during the civil war, can not serve, as evidence of depreciation of gold. The fall of the exchange rate of the dollar in Sweden or Spain during the war is explained by the support (pegging) of it to the franc and pound and by the *obstacles* of movement of gold on the world market. Once these exceptional conditions disappear, also the normal value of gold reemerged. The striking example – England since mid 1919 and the USSR in 1923.

16. World mining of gold from 1915 to 1922 including everything declined due to different causes. The cost of production of it in gold money during the war and after it until 1921 grew everywhere: prices for materials and wages rose, productivity of labour fell, finding a shortage of labour forces in some countries and of means of production, such as machines, as well as chemical agents (Russia); a prevention of an increase of mining also by the revolution in Russia and Mexico, the bloody strikes in the Transvaal. About a *decrease* of the value of gold by force of changes in the *conditions* of production there can be no talk. On the contrary, insofar as in this period the value of gold was determined by the cost of production, it too must have risen, although also less than the value of other commodities. But on the world value of the gold-commodity, as we saw, a series of factors have influence. Even if we assume that the conditions of the world market enacted a fall in the value of gold, decreasing the increase, due to the fall in productivity, of the world socially necessary labour time, applied in its production, then in the extreme case one will have to recognise that it did *not change*, but *drop* it could *not*.

Let us note further, that there was not any 'subsidy' to gold producers in the British Empire. That, what was called a 'premium' since 1919, was a difference between the exchange rates of the dollar and the pound sterling, as the *world* 'price' of gold was quoted by the corresponding world *gold standard*, which remained the dollar.

17. Analysis of commodity prices during the war shows that the revolution of *rising* prices covered in more or less degree, sooner or later, all countries of the earth, belligerent as well as distant, developed capitalist, as well as the rest and colonies, in short – *the whole world economy*. England, France, Italy, Germany, Austria, Russia, Denmark, Sweden, Norway, Canada, Australia and others detected a rise of prices already at the end of 1914; India, Argentina and the United States – in 1915; Japan – in 1916. Analysis shows that the connection between prices of European countries is closer, than between each one of them and the United States. The same is observed also now. The rise of commodity prices during the time of the war can be explained wholly by the change of conditions of commodity

production and trade: there was the shortage of commodity production, a disorder and rise in cost of transport. Commodity prices rose also by force of the inflation of credit, subject to increased state consumption demand; they rose also from the strengthening of taxes, inasmuch as the latter went into prices as an element independent from the value; there took effect also monopolistic prices. And not only the commodity prices rose by force of the deviation of them from the value of commodities, inasmuch as they could be realised with extra-profit by way of expropriation of the countries in need of commodities, and in every country of broad layers of population – but also the value of commodities rose strongly: by force of the worsening of conditions of production, the destruction of capital and the fall of labour productivity. This remained in significant degree in force also then, when in 1920 due to the commercial-industrial crisis, beginning in the East, the world economy experienced a catastrophic decline of prices, transmitted in the course of a few months to all corners of the world. The repercussion of the war time has not disappeared until now, therefore the pre-war level, – not considering particular strong inflationary countries (Germany), – for all the post-war time was not reached. The costs of the apparatus of distribution and transport increased for railways as well as for maritime shipment (also in America). The increasing production capacity in particular countries cannot be fully utilised under the present situation of the world market and bears down weight on the diminished commodity production (England, Germany). Wages rose.[302] Tariffs were raised and the number of tariff walls were increased for the whole world, which leads to the strengthening monopolist organisation with the purpose of exploiting the narrowed market by higher prices. The strengthened tax pressure, decreased the accumulated money capital in Europe and makes credit more expensive. The world undoubtedly became poorer: under a marked increase of population world production until now rose insignificantly against 1913. World production capacity is not fully utilised. The productivity of world labour decreased. The social labour time, – necessary for the satisfaction of the previous consumption of the world economy, rose, and the exchange value of commodities had to rise. The height of the world level of prices certainly is reflected on the current level of such countries as Germany and the United States, from which the latter especially now develops its productivity. America nonetheless, experiencing an extraordinary boom, does not see *rising prices*, but on the contrary,

[302]High wages – we speak here of course not about the expression in depreciated money – can take place not [just] from an increase of labour's share in the product under increased productivity, but also from an increase of its share due to a *fall of productivity*. Wages rose during the war and in the first years after it (also in the United States) as a result of the dearness of commodities from the fall of labour productivity. The mass of commodities fell and the price of each rose. This phenomenon has not disappeared in the *world* economy, taken as a whole, until now [1927].

decreasing ones. An illustration of this, that the cause of increasing level is on the side of commodities, can serve also [the fact] that in South Africa the general price level, for the last years the lowest in the world, rose by 26% against 50%, which could not be possible, if the rise of the *world* price level happened from the fall of the value of gold. This [fact] would have to take especially into consideration the quantity theorists, who see mistakenly, of course, – the proof of the correctness of their theory in the fact that prices in locations of gold mining are for the most part *higher*, than in the main world markets.

18. The quantity of gold, found in a country, does not determine the amount of money in circulation. The latter is determined by the requirement of turnover [circulation], by social demand for monetary means. The quantity of money in a given country does not determine the value of money, on the contrary, the value of money, under other equal conditions, determines the quantity of it. From the social demand depends also the extent of credit. The subjective action of bankers corresponds to *objective* conditions. Between the quantity of gold in a country and the extent of credit there is no *necessary* connection. The sum of money in circulation and the extent of credit are likewise not found in a necessary connection.

Analysis of the movement of gold reserves and of the issuance of *banknotes* in the United States in the beginning of the war until today shows that under strong *inflow* of gold there took place a *weak* issuance of banknotes; in years of *outflow* of gold there was observed a *strong* issuance of them; further there was observed strong *reduction* of money circulation under a *decrease* of gold reserves. And, finally, there was observed stability of the mass of money circulation under enduring inflow of gold. This confirms the by us shared old theory of Steuart–Tooke–Marx, that there is no direct and necessary connection between the inflow of gold and money circulation. The given shows, that the demand for means of circulation went in the United States counter to the inflow of gold, which called forth the necessity of the issuance of *fiduciary* credit money.

Analysis of the *credit system* of the USA shows, that the expansion of credit of the reserve system happened under the outflow of gold and a shortage of deposits of the member banks. And, conversely, the inflow of gold and the increase of deposits of member banks lowered the quantity of the money mass in circulation. Not the reserve bank system, but the turnover decided the question about the *utilisation* of the gold fund actively or its storage as treasure. Analysis of the inflow and outflow of gold and the movement of commodity prices in the United States during the war and after it show entirely definitively, that between them there is no necessary connection.

There is no such correspondence between the movement of world gold money *reserves* and the movement of prices in the United States in the time also after the war. There is *in general* not any *necessary* connection between world *reserves* of gold and the *world level* of prices. The given [fact] certainly refutes the position of the quantity theorists, that the prices in *single* countries and *for the whole* world change *proportionally* to the change of the quantity of gold money or world gold reserves. There is no *necessary* connection either between the world *mined* gold and the movement of prices, as this is shown by the data of the United States and England, available since 1780 until today: there is observed a rise of prices under a reduction of mining, and the converse.

19. The quantity of gold, as *money* capital, has meaning for the height of the *interest rate*, and therewith also for the compression and expansion of credit, and with this – for the movement of commodity prices, but the *phases* of the industrial *cycles do not depend* on the quantity of gold in a country. Evidently there must be the appropriate conditions of production. The inflow and outflow of gold has a different significance in different phases of the industrial cycle. So, the inflow of gold in a time of boom strengthens the latter, the inflow of it during times of crisis weakens the latter. The outflow is more dangerous during a time of crisis, than in other phases. The distribution of gold world reserves between different countries depends, under other conditions equal, on the roles occupied by the countries in the world commodity trade and credit relations. The impaired, due to the world crisis, equilibrium in the distribution of world reserves sooner or later, by the clearing of the crisis, will be restored.

20. The sums of opened credits is not found in necessary proportion with the extent of gold. They can grow also under weak reserves of it, especially under favourable conditions of the cycle. If the expansion of credit is long, standing in connection with increasing quantity of gold, which from its side is connected with the decreasing value of gold, then this decreasing value of gold exercises its effect also through credit. The change of the value of gold exercises its effect through the quantity of money and the extent of credit, but not *contrariwise*.

21. The government cannot emit into circulation more real money, than is required by real turnover, and bank credit cannot call into life more real money capital, than the social process of reproduction under given conditions is able to create [of it]. Every artificial increase of money by the government, every artificial expansion of credit revenges itself. Money calls into life the expansion of reproduction, because this possibility is given also without it. Money – and gold money – *by itself* – is not yet an element of real reproduction.

22. The laws of credit and the laws of money are not one and the same. But they influence

each other. While an inflation of credit – a general companion of the cyclical movement of industrial capital – is easily overcome so long as the money basis of the credit system is not affected, then [by contrast] a thinning of this basis, a depreciation of money, once arisen, shatters the whole economic organism, including therein also credit. The best proof of the falseness of the theory, that the money value of gold is based on credit, and not the reverse.

23. The quantity theory, explaining the quantity of money in circulation by the inflow and outflow of gold, by the quantity of money – [and] explaining the change of the interest rate, the height of the latter – by the change of the prices of commodities, is untrue. Prices can move in one direction with the interest rate, due to the different movement of productive and money loan capital. From the other side, a high interest rate can exist with low prices.

24. The movement of gold on the international market is determined: a) by the itinerancy of gold as commodity, from the source of extraction, b) by its movement as means of international commodity trade and in the quality of exported money capital, which stands in connection with exchange rates, reflective of the international balances of payments and relation of interest rates of different countries and, finally, c) stands in connection with the violation of the money system in one or another country. The claim that the price level is striving in the whole world to become *one and the same*, and that the inequality is corrected by the export and import of gold is untrue. Prices have only a tendency to *fluctuate in one* and the same direction, but they are not *one and the same* in different countries. All commodities carry *first of all* a national character and have a national value, only gold – the genuine world commodity also enters the national sphere with a *world* value.

25. Both under a stable, gold currency with constant parity, and under an instable, paper [currency] with variable centres of equilibrium (parities), the currency parity being determined by the relation of the value of the currencies of the compared countries, the value of these currencies is determined [by] the *world* value they represent of the universal commodity gold, that is by *the weight* of gold enclosed in them. There where silver serves as money, there its parity with the gold monetary system, and with it also the exchange rate, changes in dependence on the change of the relation of the value of gold and silver on the *world* market. The currency parity does *not* depend on the *commodity* prices or, otherwise, on the purchasing power of money. Fluctuations of exchange rates around the parity happen by action of the balance of *payment*, no matter what had caused the change in the latter. Not the rate of exchange is based on the prices of commodities, but [on the contrary] the prices adapt to it, wherewith between the movement of prices and the movement of exchange rates there is not an exact adaptation. The latest study of the movement of prices and of the rates of

exchange in India from 1873 to 1924 shows the correctness of the by *us* defended theory.[303] The detailed chart [p. 278] of the exchange rates of the rupee in relation to the pound sterling and of the value [price in pounds] of the silver enclosed in the rupee from April 1918 to March 1921, shows precisely a correspondence between the bullion value [price] of the rupee and the exchange rates: the rise of the exchange rates from April 1918 to the end of February 1920 and the fall of the exchange rate from February 1920 until February 1921 corresponds with the bullion value [price] of the rupee. The analysis of this movement of the exchange rate of the rupee in relation to the pound sterling and to the purchasing power parity for all the given fifty years does *not* confirm the theory of purchasing power parity.

Conclusions

1. Gold is the commodity most stable in value that can serve as fundament for the modern money–credit system. Gold is the steadiest measure of value.
2. Gold money is not ideal money. Such money there is not and cannot be. Money changes over time: together with the change of the value of gold. Its purchasing power also changes: in connection with the change of its own value as well of the value of commodities.
3. The gold standard is invariable by weight, the most steady by value. Such standard is the steadiest also from the viewpoint of the purchasing power of money, in which enter two variable magnitudes. The world understood this: having gone through a period of inflation and currency chaos, it, having rejected any projects of a variable, scientifically-regulated standard, has returned to the tested in life gold standard.
4. The modern plan (Lehfeldt 1926) to regulate the mining of gold with the goal of stabilisation of its value in long periods is not new (A. Wagner, Marshall). Inasmuch as this is caused by fears for the position of the value of gold, in connection with the possible flooding of American gold, they rest on the false quantity theory of money (Fisher, Cassel). Inasmuch as it is alleged that the revolutionary fall of the value of gold and the increase of its quantity had catastrophic effects in world economic history (Keynes), this does not correspond with reality: on the contrary, they facilitated economic progress. Inasmuch as by such regulation the task is put foward of the stabilisation of purchasing power, it is utopian and not at all suitable for its intended purpose. The pros of the stabilisation of commodity prices in capitalist society are outweighed by the contras: it weakens the regulator of production and stirrer of its expansion. The theory, which identifies the stabilisation of prices with the

[303]Narain 1926.

stabilisation of production, is wrong.[304] Concern for a rise of the value of gold is based partly on contradictory, and partly confused predictions of mining engineers about [running out of] world reserves, which until now were not justified, or on calculated statistics, which now already have brilliantly failed (for example – Kitchin). As regards the rise of demand for gold with the transition of the majority of countries to gold circulation, then the experience of the past decades shows, against the warnings of the bimetallists, that the capitalist economy was able until now to adapt, based on the existing reserves and the developing credit system.

5. From the three forms of gold money systems, most satisfying of the needs of a stable currency externally and internally is a *banknote–gold* [system of] circulation. The development of credit and cheque turnover and so on, reduces also in such money system the circulation of gold internally to a minimum. Such gold money system, besides the United States, was implemented for the last years by South Africa, the Netherlands, Sweden, to this are striving Germany, England and others. For poorer and remaining countries the best of all is a *gold–ingot* circulation, requiring less gold, as it manages without gold internally, and protects from hoarding by its population (conclusion of the 1926 Royal Commission on Indian Currency and Finance). And, finally, the third: a *gold–foreign exchange* [system][305] has on first sight the whole advantage that it does not require expensive instruments of circulation – gold – internally and idle lying gold reserves; the corresponding means can be placed in foreign currencies bearing interest (Mises). However the in this system *prevailing* strong defects entail that it is more difficult to regulate and is [a form of] *vassalage*. It is characteristic, that *sovereign states*, taking into account the benefits of a full–gold circulation, are willing to make (and *made*) 'sacrifices', decreasing accordingly *their* gold reserves. (To this also Cassel points.) No *independent* country will forgo on such allurement.

[304]As this understands also Robertson (1926).
[305][The so-called gold exchange standard.]

Chapter Eighteen

Review of Ludwig Mises, *The Theory of Money and Credit* (27 September 1912)

Rudolf Hilferding

The gentlemen of the marginal utility theory have a high opinion of their doctrine, which they also transfer to representatives of the doctrine – a psychological process that indeed usually takes place in opposition to those observed by the school. They are imbued with a true revelation of faith, and even the nearly forty years of wandering in the wilderness of fruitless speculation on such a belief cannot change anything. And indeed, this doctrine seems to be immortal; it has a kind of potentiated immortality. The school lives, so to speak, of suicide. Each marginal utility theoretician infallibly begins by conclusively demonstrating the serious errors which his school committed before him, and the reader gratefully pronounces his *Requiescat in pace* [rest in peace]. To this positive part follows a negative one, in which the happy annihilator provides his successors with some substance for the same exercise. And thus the series never end. In pious Austria, memorials have been erected in remembrance of every such disaster: lecturing posts and professorships mark the Calvary that the school went through since Carl Menger invented it freely after Hermann Gossen, and decided with Böhm-Bawerk on the occupation of the universities. Because the marginal utility school is an admirer of monopoly not only in theory. It knows how to assess its power in practice; in fact one could even consider this as the only bond that connects it with reality. Among the unresolved problems of the school – and unresolved are all its problems – the money problem naturally occupies a prominent position. It is the true cross for these theorists, under whose burden they have all collapsed, without such a collapse resulting in a release for erring humanity. The question is: How is the exchange ratio between money and commodities determined by the subjective theory of value? The 'value' of the product is given by its marginal utility, that is by the utility that I attach to the last part of the quantity of a stock. So, to use the famous example, which so faithfully reflects the processes going on every day on the world market: if I have a sack of grain, I will attach very high value to it, because it is essential for the satisfaction of my vital needs; if I possess, on the other hand, five sacks, I will attach to the fifth, which serves me to feed parrots – because my other grain needs are already met by the other four bags – a much lower value. This estimate of the fifth sack, the last quantitative part of the available stock, is the marginal utility, and it now determines for the lucky owners the value of the grain. But what about the marginal utility of money? The

utility of money is nothing but the value of the goods that I get for the money. Or, as expressed by professor Wieser: 'The exchange value of money is the anticipated use-value of the things to be acquired by the money'. But how many goods I get, again depends on the 'value' of money, that is on its utility. It is a vicious circle.
The merit of Mises' is that in the first (positive) part of his work he shows that the previous attempts at value measurement by the 'psychological' school ended up in failure. He finally formulates the embarrassment which the subjective value theorists feel as follows:

> Consideration of the subjective value of money without discussion of its objective exchange-value is impossible. In contrast to commodities, money would never be used unless it had an objective exchange-value or purchasing power. The subjective value of money always depends on the subjective value of the other economic goods that can be obtained in exchange for it. Its subjective value is in fact a derived concept. If we wish to estimate the significance that a given sum of money has, in view of the known dependence upon it of a certain satisfaction, we can do this only on the assumption that the money possesses a given objective exchange-value. ... Whenever money is valued by anybody it is because he supposes it to have a certain purchasing power.[306]

The bankruptcy of the subjectivist theory of value, its inability to explain the fundamental problem of economics, cannot be more clearly stated. But when the theory is sick, the history sits down at the table. We get to hear a fable from the grey past. 'A valuation of money is possible only on the assumption that the money has a certain objective exchange-value. Such a *point d'appui* (!) is necessary before the gap (!) between satisfaction and 'useless' money can be bridged'. (The wealth of images reveals only the vagueness of the concepts. If the exchange value of money is given, then there is no room for a subjective estimation. Instead of a '*point d'appui*' we would have a sure determination, but at the same time also an unchanging monetary value. But Mises cannot want that, as we shall see.) Since there is no direct connection between money as such and any human want, individuals can obtain an idea of its utility and consequently of its value only by assuming a definite purchasing-power. But it is easy to see that this supposition cannot be anything but an expression of the exchange-ratio ruling at the time in the market between the money and commodities.

Once an exchange-ratio between money and commodities has been established in the

[306]Mises 1953, pp. 98–9.

> market, it continues to exercise an influence beyond the period during which it is maintained; it provides the basis for the further valuation of money. Thus the past objective exchange-value of money has a certain significance for its present and future valuation. The money-prices of to-day are linked with those of yesterday and before, and with those of to-morrow and after.
> But this alone will not suffice to explain the problem of the Element of Continuity in the value of money; it only postpones the explanation.

Very true! And, get ready for it:

> To trace back the value that money has today to that which it had yesterday, the value that it had yesterday to that which it had the day before, and so on, is to raise the question of what determined the value of money in the first place. Consideration of the origin of the use of money and of the particular components of its value that depend on its monetary function suggest an obvious answer to this question. The first value of money was clearly the value which the goods used as money possessed (thanks to their suitability for satisfying human wants in other ways) at the moment when they were first used as common media of exchange. When individuals began (!) to acquire objects, not for consumption, but to be used as media of exchange, they valued them according to the objective exchange-value with which the market (!) already credited them by reason of their 'industrial' usefulness (but, please, more precisely, how much? That would be very important!), and only as an additional consideration on account of the possibility of using them as media of exchange. The earliest value of money links up with the commodity-value of the monetary material.[307]

What a moving performance! If we purchase at [neighbourhood delicatessen] Aschinger's a ten-penny bread roll, then we find ourselves in a previously secret, but finally revealed connection with the past. We are not reminded of it, for instance, by the hardness of the bread roll; not its vile use value, but its objective exchange value brings us in direct connection with those times, when for the first time a barbaric ancestor took a gold ring from his chest to purchase a cow with that money. Or must we go back even further? Is there not between the cowry money or the cattle of money and the gold money a 'recurrent connection' [*rekurrenter Anschluss*], as Knapp would say? One can see that the history of the school is at

[307]Mises 1953, pp. 109–10.

the same level with its psychology!

Unfortunately, Mises does not linger long on his idea of making the psychology of primitive times the precondition for the economic assessment of living economic subjects. He hastens to leave his '*point d'appui*' and build a bridge to the present. Although he recognises that between the formation of the exchange value of money and that of other economic goods a fundamental opposition exists (p. 111), which in reality is a fundamental contradiction between his 'historic' deduction of the value of money and the psychological foundations of the theory, whose coherence is broken if the exchange ratio is not determined by the estimations of living agents, but partially (and for what?) by long-ago deceased ones. But for the further progress [of marginal utility theory], this 'objective' value of money, arisen from the grave, has no meaning. For 'the historically-transmitted value [of money] is transformed by the market without regard to what has become its historical content' (p. 114). That happens like this: The money supply of the economy is changing, let us assume that it is expanding. This

> always means an increase in the amount of money held by a number of economic agents, [these may be either] the issuers of fiat [*Zeichen*-] or credit money or the producers of the substance of which commodity money is made. For these persons, the ratio between the demand for money and the stock of it is altered; they have a relative superfluity of money and a relative shortage of other economic goods. The immediate consequence of both circumstances is that the marginal utility to them of the monetary unit diminishes. This necessarily influences their behaviour in the market. They are in a stronger position as buyers. They will now express in the market their demand for the objects they desire more intensively than before; they are able to offer more money for the commodities that they wish to acquire. It will be the obvious result of this that the prices of the goods concerned will rise, and that the objective exchange-value of money will fall in comparison. (p. 139)

We had just heard that: 'Since there is no direct connection between money as such and any human want, individuals can obtain an idea of its utility and consequently of its value only by assuming a definite purchasing-power'. Now a change in the amount [of money] directly changes the marginal utility. The logical circle, which Mises demolished historically, is now theoretically happily closed again.

Here, the whole structure is totally arbitrary. A, who earlier had 100 marks, now has 200. He knows the historical exchange ratio [between money and goods], and there is for him no

reason to depart from it. If my supply increases from 1 to 2 suits, the marginal utility diminishes. Not so with the money. The marginal utility of money is exactly equal to the marginal utility of what I can buy with it. The marginal utility of the suit has not changed by the fact that my money supply has doubled. If 100 marks were equal to a suit, so now 200 marks are equal to two suits. Nothing leads me to give for the suit more than before, because for the seller of the suit its marginal utility has not changed, he will leave it to me at the old 'historical exchange ratio'. Mises saves himself from the embarrassment by simply having recourse to an explanation based on the relation between supply and demand. If he wants to say only that, with increasing wealth, more things are in demand, that is self-evident. That an increasing in demand may temporarily lead to an increase in prices, is also not unknown. In that case, production is increased until, all other circumstances being equal, the old price level is again restored. A permanent change in the exchange ratio is not explained by this.

But since Mises in this way, as it is inherent in the nature of the marginal utility theory, after a long detour finally goes back to explaining economic phenomena by means of the relationship between supply and demand, he lapses completely back into the old quantity theory, whose conclusions he not only does not accept, but whose errors he even exaggerates. It is unnecessary here to follow him into the details. It is outright comical when Mises, for instance, berates the capitalists because they do not consider the constant changes in the value of money in their businesses. Even more comical, because Mises himself cannot say how they should do that, and it is for this very reason that both Thyssen and [Deutsche Bank director] Gwinner will also in the future refrain from doing business on the basis of marginal utility theory.

For curiosity's sake, we should only note that Mises, as a consequent quantity theorist, believes that the banks can increase the means of circulation arbitrarily and indefinitely. Since he shares Böhm-Bawerk's view that interest depends on the size of the national subsistence fund, it is impossible for him to find the specific determinants of the level of monetary interest. He therefore comes to the absurd conclusion that the banks, by reducing the rate of interest in their lending business, can increase immeasurably the demand of the public, and also satisfy that demand by increasing their emissions of means of circulation. And this is, according to Mises, a serious threat to capitalism. The modern organisation of exchange 'carries within itself the germ of its own destruction; the development of the means of circulation must necessarily lead to its breakdown' (p. 409). And this latest breakdown theorist lets us off with the comforting assertion that 'there are problems that may lead beyond the individualistic organisation of production and distribution to new, perhaps

collectivistic organisational forms of the social economy'.[308] So about this no enmity!

It's a pity what happened to Mr von Mises. He is a knowledgeable writer, as proven by his, in parts, excellent study on 'The problem of the legal resumption of gold payments in Austria-Hungary'.[309] In the above-reviewed book we also find in [questions of] detail some interesting remarks. That is why this book, in its utter inconclusiveness, is the best evidence of the total barrenness of the marginal utility theory. Just because Mises, with logical consistency, but with indifference to the correspondence with reality, draws all the conclusions from his assumptions, the result was condemned by the false starting point, the subjective theory of value.

[308][Page 476 original edition, not included later.]
[309]Published in *Schmoller's Jahrbuch* 1909. [See Mises 2012.]

Chapter Nineteen

Nominalism and the Problem of the Value of Money (1928)

Grigory Dashevsky

Nominalism, as also any consistent theory of money, must fit in some more general conception of the economy and therewith reveal its position in relation to the basic problem of money – the problem of its value.

It seems to me that we are not mistaken if we point out *the closest connection of nominalism with the psychological conception of economy, especially with the theory of the Austrian school*.

The most prominent representatives of modern nominalism – Knapp, Elster, Bendixen, Liefmann and others – are subjectivists.[310] Being, on one side, the logical extension of the theory of the Austrian School, which passed by until this day the problem of money, nominalism, on the other side, has common roots with the *theory of relational value of Bailey*. 'Value denotes consequently nothing positive or intrinsic, but merely the relation in which two objects stand to each other as exchangeable commodities'.[311] Nominalists likewise do not recognise value as a quality immanent to the very nature of the commodity; the value of a commodity is something relative. But if the commodity fetishist Bailey considers value as *a relation of things to things*, the psychological fetishists consider value as *a relation of men to things*,[312] as a mental condition, caused by the exposure of things to the evaluating subject's mind.

> The value of commodities does not lie in things, but in *human representations* ...

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[310]The contention of this may seem somewhat paradoxical for Knapp, but we ignore in this case the objective legal constructions of Knapp and emphasise only those aspects that bring him together with the, so to speak, 'economic' nominalists, and these aspects, according to us, boil down to the deep psychologism of Knapp in the conception of economic phenomena. It is hardly necessary to specially prove that in the conception of the problem of value and even the conception of the exchange rate ('The inter-valutary exchange ... is a psychological phenomenon', Knapp 1924, p. 221). Knapp is a proponent of the psychological conception of economy.

[311]Bailey (*Critical Dissertation*, pp. 4, 5) cited in Marx 1989b, p. 327.

[312]Explaining his conception of value in § 20 of *The state theory of money* (An ill-fated subchapter! The epigones of chartalism try to present it as an artificial and failed construction of Knapp, not having any connection with his conception as a whole), Knapp refers to § 8 of Schopenhauer's *Grundlage der Moral*. 'Each "worth" [value] is a valuation by comparison in two ways: First, it is relative, since it exists for some one (*dann erstlich ist er relativ, indem er für jemandem ist*), and secondly, it is comparative, as being compared with something else, and estimated accordingly. Severed from these *two* conditions the conception value loses all sense and meaning'.

From these excerpts it is clear that nominalism is inclined to synthesise the presentation about value, as people's attitude towards things, with the presentation of value as a relation of things to things (Bailey). *In fact*, as we will show later, nominalism knows only the second *derivative* relation, because the basic relation includes in itself the riddle of the universal equivalent, completely incomprehensible for nominalists.

> The value of things is a consequence of cognitive human activity.[313]
>
> In political economy there is no relation between things, but only a *relation of things to people*.
>
> Therefore there can be no exchange relation between money and goods, but only a "relational assessment", so to speak, an individual relation of each person to goods on one side, and to money on the other.
>
> From these relations, consisting in comparison of utility and costs, stems the economic relation of people ...[314]

The logical consequence of the assumptions of commodity fetishist and psychological theories of relational value is the *identification of price and value*.

Arguing that exchange value is the relation of two objects, exchanged as commodities, Bailey takes as a starting point the 'superficial form of exchange value, that is, the quantitative relationship in which commodities exchange with one another'.[315]

Nominalists likewise proceed from the finished money form of the commodity. The problem of the formation in the subject's mind of the price of commodities is at the same time the problem of the formation of their value. Thus, value and price are the result of the same mental act. The problem of value completely drops and is replaced by the problem of price. Indeed, the terms 'value' and 'price' are used in most cases by nominalists indifferently.

Thus, the connection between nominalism and the theory of relational value of Bailey is beyond doubt.

Let us consider now in a few words the connection of nominalism with the theory of the Austrian School.

The Austrian school, proceeding from a single individual economy, from the so preferred in bourgeois economy Robinsonade, still somehow solved the problem of the direct exchange of goods. But how to explain the phenomenon of circulation, the phenomenon of money economy, what are the determining principles of the value of money – that is the question which the Austrian School until this day tried to pass by.

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[313]Bendixen 1912, p. 21.

[314]Liefmann 1916, p. 101. Of course, neither Bailey, nor the nominalists are right. The value of commodities is not a relation of things to things or of people to things, but *the relation of people to people*. In this sense the recognition for the commodity's value of the property of 'absolute' value does not at all mean that value is really absolute. Absolute value also is relational but in the sense that it expresses the relation of individual labour time to the labour time socially necessary for the production of the commodity. But it is absolute in the sense that its existence does not depend on the material properties or the amount of certain commodities; value is the spirit of the commodity, the change of its bodily shell is the change of its form of manifestation. In distinction to the infinitely varied relational form of its manifestation, value, as social substance of the commodity, is absolute.

[315]Marx 1989b, p. 326.

Indeed, if the value of commodities can be considered as the result of individual psychological assessment, based on the use properties of purchased commodities, then what use value has money, as a result of what subjective psychological states does there arise in the mind of the subject a particular representation about the value of money?[316] This question the Austrian School was not able to resolve.

Such a pillar of the theory of marginal utility, as Menger, adjoins, for example, partially the metallists; for Menger, the value of money should follow from 'the value of its material and coinage'.[317]

From the point of view of Menger the value of money is due to its use-value as metal, but whereas the use-value of other commodities is transitory and disappears with the passage of commodities from the sphere of circulation into the sphere of consumption, the use-value of money is inherently linked to its function as *instrument of circulation*.

Thus, the theory of value of metallic money of Menger is dualistic: on the one hand the value of metallic money derives from the technical-use properties of the metal, on the other from the function of money as an instrument of circulation. Even more unsatisfactory is Menger's solution of the problem of the value of paper money. The question of the value of paper money he simply passes by and only in one place contents himself with the remark that the value of paper money 'like all other property papers, found in circulation, derives from the value of right, connected with ownership'.[318]

Here value is derived from other values, also floundering still in explanation and definition, an economic concept is derived from a legal concept.

The rift between the theory of paper and metal money discloses the weakness of the reasoning of Menger, considering through a psychological perspective money not like an abstract unit of account, but like a commodity.

The question of how from the subjective *mediated* assessment of commodities (because in a commodity-money economy between subject and object stands money) emerge objective prices, not dependent on the individual economic subject's relationship to things, but, in contrast, *determining* the psychological assessment of things, this question Menger also was not able to solve.

'Knowledge of price for the act of assessment is necessary and sufficient, just as much as the employment of a unit of value is superfluous and useless (for measuring the value of a

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[316]'The use value of gold as money is to represent exchange value' (Marx 1987, p. 361).
[317]Menger 1950, p. 260.
[318]Menger 19, p. 260.

commodity. – G. D.)'.[319] But does this recognition not mean the bankruptcy of Menger's psychological conception, related with the commodity understanding of money, as a commodity, before the problem of the assessment of price?

In the same *circle vicieux* as Menger, Böhm-Bawerk and other theorists of the Austrian school fall. For example, Böhm argues that the *subjective* exchange value depends: 1) *on the objective exchange power of things*, 2) *on the nature and extent of need* and on the property status of the owner.[320]

In this way, the theory of money and its value in the Austrians is developed very unsatisfactory and represents the most vulnerable place in the system of the Austrian school. 'The theory of money of the Austrian School plainly reveals the entire theoretical barrenness of all their constructions — their complete theoretical bankruptcy'.[321] In the frame of this article we cannot stop in greater detail at the theory of the value of money in the interpretation of the Austrian school. Let us only point out that the failure of the psychological direction in political economy to couple its conception with the phenomenon of money circulation, has caused among some proponents of the school doubt, to what extent the general theory of marginal utility is applicable to the theory of money. Already Wieser expressively indicates the gaping hole in the theory of the Austrian school. Wicksell also stated the view that the conception of marginal utility applies only for the explanation of relations arising between directly exchanging goods; that as concerns the relation in which money and goods exchange, it is completely unable to explain it.[322]

Trying to bring the Austrian school out of this impasse, in which it came, nominalism above all decidedly rejects Menger's conception of the commodity nature of money. In fact, it is easy to see that the recognition for money of the quality of commodity is in irreconcilable contradiction with the theory of marginal utility and must inevitably lead to eclecticism and internal discrepancies. Denying the substantial value of money and its commodity nature nominalism consistently develops the psychological conception of the economy in the theory of money – in this sense logically bringing the theory of the Austrian school to a close.

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In *A contribution* Marx gave a comprehensive and deep criticism of the theory of the

[319]Menger 19, p. 297.

[320]Although the Austrians, as well as the nominalists, in words start from a pure-psychological subjective conception of the economy, without noticing it they will accept in their conception social, objective elements. Like Menger and Böhm-Bawerk, the nominalist Liefmann puts the individual psychological assessment of commodities in dependence on the objective existing money price of commodities.

[321]Bukharin 1927, p. 96.

[322]Wicksell 1936, p. 18. So also pessimistically expressed Helfferich. While Mises, quite the contrary, wrongly believes that both assessments of money, based on 'real' and 'circulating' – to use the terms of Knapp – properties of money, can in equal degree apply the law of marginal utility (Mises 1924, p. 101).

'nominal standard of money' [die Lehre von der *idealen Maßeinheit des Geldes*], reborn in the twentieth century under the name of nominalist theory. Which objective phenomena of economic life constitute the subsoil of the nominalist system, where are its economic roots? It seems necessary to emphasise *three* moments here:

1) If nominalists of that era, when kings spoiled coin, trying to gather in their crucibles its excess fat, justified their views on the fact of the historically only emerging gulf between the function of measure of value and the function of means of circulation, the nominalists of twentieth century take as the basis of their theory the juridical form of this splitting of money – paper money.

We know what a strong influence on the nominalists (in significant degree as well on Hilferding, Tugan-Baranovsky and others) the existence was of the paper-money system in Austria.[323] The inability of the commodity metal theory of money to explain the phenomenon of paper money circulation led to the other extreme – to the desire to throw a paper-money cover onto the essence of money, in its basis being materially congealed universal labour.

From the fact that money in prominent functions of it can be replaced by signs, nominalism concludes that money in its own essence is only a sign and cannot derive its value from its nature, as commodity. Contrasting money to commodities, as two poles mutually exclusive to each other, nominalists refuse to understand that the contradictions of the commodity can be solved with money only if it itself is a commodity. Nemo contra Mammon nisi Mammon ipse.

2) The other moment, besides the growth of paper-money currency in all the capitalist countries, is the unprecedented development of international and internal-economic *moneyless accounting, giro circulation*. The separation of money into its symbolic form of existence takes place at a higher level of socio-economic development, characterised by the growth and consolidation of credit relations.

How quickly non-cash settlements develop in the era of monopoly capitalism, in the era of powerful growth of bank capital and bank transactions, is shown by the following information:

Transactions of the Reichsbank[324] (in billion gold marks)

1891	1913
Through giro-transaction:	
81,1	379,2
Through settlement transactions:	

[323][Another case was the Argentine peso at the turn of the century. For a critique see Justo 1937, pp. 74–5.]
[324]According to Schulze-Gaevernitz 1915.

17,6 73,6

Total: 98,7 452,8

Cash settlements as a percentage of total turnover:

24.7% 9.6%

Thus, the role of cash settlements over 22 years fell 2,5 times. And it should be noted that in Germany, moneyless transactions are less developed than in England and the United States. In the Uinted States in 1871 payments with cash banknotes and metal coins made up only 12%, while 88% with cheques and promissory notes. In 1881, all sorts of moneyless transactions settled already 92% of all payments, and then later, this percentage has still increased...

On the development of non-cash transactions during the war, England gives a wealth of material. Transactions by mutual settlements of London and provincial banks constituted:

1914.	14.665	mil.	£.
1915.	13.408	“	“
1916.	15.275	“	“
1917.	19.121	“	“

1918. 21.198 “ “[325]

But credit documents, which are means of moneyless operations – promissory note, cheque, remittances in their various forms and types, – appear at first glance only like an *ideal set of abstract computing units*. The development in the world economy of moneyless accounting unwittingly pushes bourgeois economists to the idea that money, by its very essence, is no more than an abstract accounting unit, in which the value of goods and services is measured. And, in our opinion, it is not at all a coincidence that the prominent representative of 'economic' nominalism, Bendixen, was at the same time a major bank figure.

Hence also the idea of the possibility of the organisation of a non-cash economy, of world *kontokorrent* accounting [current accounts], *comptabilité sociale*, in Schumpeter’s expression, in its development leading to the idea of labour money. On the other hand, since the credit relation, emerging from the spontaneous capitalist economy, suggests the presence of *organised* connections, of known *agreements* between the participants of payment turnover, the development and growth of non-cash settlements calls forth in the

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[325]Kuyerman 1927, pp. 33, 34.

nominalists the view of the world monetary economy, as a grand clearing house; and the idea of money as a category of *organised* society. *Circulation is replaced by an organised exchange*, the money mass is opposed to the commodity 'heap'.[326]

In this way, nominalism is not only a paper-money, a symbolic, but also a *credit* theory of money, which has found its further development and completion in the well-known credit theory of L. Albert Hahn.[327]

That is why nominalists dissolve money in the concept of *means of payment*, and the latter in its turn (we will attempt to prove this with the example of Knapp) in the concept of money. This is the specific novelty that nominalists introduced in the theory of the 'nominal standard of money', which Berkeley, Lowndes, James Steuart and others had developed in their time.

3) Finally, the third moment, related to the development of monopolistic tendencies in modern capitalism, is the presence of a *limiting monopoly* in the sphere of the price formation of metals. Hence the idea that money does not get its value from gold and silver, but on the contrary, gold and silver get their value from money. Hence the peculiar theory of the intervaluta courses, which boils down to the point that the value of gold and silver is determined by the status of inter-currency parities, which in turn, is caused by the authoritarian exogenous action of the government.[328]

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[326]Most clearly this is expressed in Schumpeter.
'If, – Schumpeter writes, – in place of money, some central authority were really to issue receipt vouchers for productive contributions, and these receipt vouchers were at the same time claim tickets on the consumption fund of the economy, then we would have before us one of the possible forms of social clearing system (a comptabilité sociale like Solvay's). For this reason the monetary circulation is in its nature and main function in the market economy nothing but a *clearing house* which is both: 1) automatic and 2) very primitive and subject to countless shortcomings and abuses' (Schumpeter 1956, pp. 154–5). Thus, the sole difference between signs issued by a central authority under organised economy, *directly* expressing claims to a certain part of the national economic consumer fund and contemporary money, is the higher perfection of the first system to the second! With the above excerpt from Schumpeter it is not uninteresting to show the following quote from Knapp: 'When we give up our coats in the cloak-room of a theatre, we receive a tin disc (Platten) of a given size bearing a sign, perhaps a number. There is nothing more on it, but this ticket or mark has legal significance; it is a proof that I am entitled to demand the return of my coat. When we send letters, we affix a stamp or ticket which proves that we have by payment of postage obtained the right to get the letter carried. The "ticket" is then a good expression, which has long since been naturalised, for a movable, shaped object bearing signs, to which legal ordinance gives a use independent of its material' (Knapp 1924, p. 31). The comparison of money with a ticket, with a certificate for *determined* concrete goods or services, shows the complete misunderstanding by the nominalists of the nature of money. A number from a cloak-room, a post stamp, etc. indicate our right to make certain demands to the central authority, issuing these obligations. 'Labour money', personifying *directly* the labour expended by participants of the economy, would be such a ticket, testifying about a right to the presentation of certain claims to the organ, managing the social fund. But this does not at all relate to money as such.

[327][See the article of Atlas in this volume.]

[328]This question was developed in detail in the article by Eidel'nant 1926. It should be noted however, that the contradiction in the economic structure of capitalism causes a contradiction also in the nominalist theory of intervaluta courses. In international settlements act not only credit documents, read at ideal counting units, but also *gold*, serving for the repayment of the saldo on the account balance. You can even say that in the era of monopoly capitalism, money *practically* performs primarily in the function of *world money*. Hence among some the idea of the possibility of an *ideally* existing money in the form of kontokorrent [current accounts]

To this we limit our extremely abridged analysis of economic factors, which created fertile ground for promoting nominalistic ideas and return directly to our topic – the formulation of the problem of the value of money in the theory of nominalism.

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Denying the commodity nature of money, nominalists consistently arrive also at the denial of the value of money. This follows already from the psychological conception of the nominalists, according to which value arises from the evaluation by the person of the object as a consumer good.

But since money is not a consumer good, because the essence of it – is not a material substance, but an *abstract unit of account*, it is impossible also to establish an independent value relationship between money and people.[329] The problem of the value of money is either completely eliminated (Knapp), or finds resolution for itself in the attempt to derive the value of money from the value relations of the whole commodity world opposing it (Simmel, Schumpeter, Bendixen). However, not recognising an independent value for money, nominalists see themselves forced to reconcile their view with *the real fact that money nevertheless measures the value of commodities*. But how can you measure a certain property, common to two objects (in this case value) by a body, which does not possess this property? In fact, can one measure the length of any object by a body, not possessing the property of extention? A man who showed a willingness to measure a given period of time not with hours, but with yards, would be considered insane. But how to take nominalists, who consider it possible to measure the value of two objects by a substance devoid of value? *Hic Rhodus, hic salta*. And it must be said, that, despite the utilisation of the *theory of proportional measurement*, the theory of relational measurement, nominalism jumps over this conundrum by smashing its forehead to pieces.

Still Jean Buridan in his work published in 1489 *Quaestiones super decem libros ethicorum Aristoteles ad Nicomachum* claimed, that for the measurement of objects it is not always necessary to use things, having the same properties as the measured items.

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settlements, the view about money in the world market as about a *commodity*. Knapp does not notice what the fact that on the world market the commodity nature of money breaks through its symbolic shell, shows about the fundamental difference between money and tickets. Money – if it were only a ticket – could be of any value abroad only by the agreement of governments, only in the case of the establishment of an international money system, similar to the Universal Postal Union.

[329]"The question about the value of money is not the subject of modern books about money. If value is understood as purchasing power, then in reality the issue is about *price*, and not about the value of money. If, however, the subjective value of money is spoken of, that is of the psychological assessment of money by the individual, then again a mistake is committed; because such a psychological evaluation in practice does not exist; it exists only in the systems of the theorists of value. The so called evaluation (*Wertschätzung*) of money is nothing but the assessment of the commodities which I get by means of money. Nobody perceives the value of money, as value independent of the prices of commodities' (Bendixen 1920, p. 30).

> An ounce measures a weight, a quarter measures a barrel of wine, a cubit measures a scarf, and so on. On this Aristotle speaks in the tenth book of his *Metaphysics*. These measures exist of the same property with the measurable things ... Otherwise is the case with the measurement of *alike relations*. (Italics mine. – G. D.) For example, motion can be defined as space, and also time, because if the motion a happens in time b, but the motion c in time d, then we conclude: a : b = c : d or, rearranging the members of the proportions, a : c = b : d. If time b is twice as long as d, then also motion a is double motion c.
>
> In an equal way one can get a result, when motion is measured by extention. So, I would argue that human need measures objects of exchange by similar proportion, and not by their quantitative comparison.[330]

Thus, in order to measure *the relative importance* of two values [amounts], we do not need to directly measure them by a scale of the same property. The latter would be necessary only to measure *absolute* value; for our purpose it is enough to know the ratio of two different values, that are qualitatively different from the first two, but conjugated with them by a known dynamical dependence.

From the contemporary nominalists the most original proponent of the theory of 'proportional measurement' of the value of commodities is *Georg Simmel*.

Let us consider in some more detail the reasoning of Simmel. Simmel refers to the well-known psycho-physical law of Weber and Fechner (in order that the intensity of a sensation may increase in arithmetical progression, the stimulus must increase in geometrical progression). Here the relative magnitude of sensations is measured not by comparing them directly, but by order of proportional connection to the relations of stimuli.

> The quantities of different object can be compared only if they are of the same quality; wherever measurement is done by *direct* comparison of two quantities it presupposes identitical qualities. But wherever a change, a difference or the relation of two quantities is to be measured, it is sufficient for their determination that *proportions* of the measuring objects are reflected by the proportions of those measured; and there need be no qualitative identity of the objects.[331]

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[330]Cited in Diehl and Mombert 1923, p. 41.

[331]Simmel 2004, pp. 132–3. [Another review is Schmidt 1901.]

Let us consider the arguments of Buridan and Simmel.

First of all about motion. Motion occurs in space and time. To measure motion, is possible therefore by both time and space. The ability to measure is already given by the objective fact of the *real unity* of motion, of time and space. Movement outside time and space is a *contradictio in adjecto*, unadulterated nonsense. Buridan, strictly speaking, has in sight not the measurement of motion, as such, in the unity of motion, but the measurement of time in relation to the space, traversed by the moving body.

The possibility of measuring the relationship of space related to time is due to the presence of a known regular connection between the two – qualitatively different – proportions; this regularity is based, as we have already pointed out, on the fact that like the relation of space, the relation of time is a different aspect of one and the same substance – motion. We have here a difference in unity.

Let us turn to the psycho-physical example of Simmel.

For the idealist Simmel the phenomenon of psychic life covered, of course, by a mystical shell, appears to be something substantially different from the effects of the material world. For Simmel, the motions of matter and the states of consciousness are 'the most heterogeneous objects we know; the two poles of the world view which neither metaphysics nor natural science has succeeded in reducing to each other'.[332]

Simmel does not understand that the relation of stimulus can only measure the relation of sensation because between the one and the other there exists some regular connection, due to the fact that sensation, as well as stimulus are forms of the same substance – *matter*. The ability to measure the relative magnitude of sensation with proportions of stimuli is given by the fact that in nature, objectively, there is a real regular connection between changes in the magnitude of sensation and changes in magnitude of stimulation – the first magnitude as function of the second. No one would dream of measuring the relation of the power of turbine generators with the relation of the amount of shoes or with the relation of the amount of eaten pies, as between these series there is no dependence at all.

What regular connection exists between money – the measuring substance and the value of commodities? Let us see how Simmel approaches this issue.

Based on the presuppositions of the quantity theory,[333] Simmel puts forward the following

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[332]Simmel 2004, p. 132.

[333]'We assume a very general relationship between the quantity of goods and the quantity of money, which is illustrated by the connection – often obscured or disrupted – between an increasing supply of money and rising prices, an increasing supply of goods and falling prices' (Simmel 2004, p. 133.). *This empirical perception of the quantity conception is extremely characteristic for nominalism*. Both theories deny the substantial value of money, derive the value of money from the value of goods, identify value with price and limit the whole field of their research to the problem of *changes* of price of commodities, avoiding the cardinal question of

postulate: 'If the commodity *n* relates to the sum *A* of all saleable goods, as the money unit *a* relates to the sum *B* of all available money units, then the economic value of *n* is expressed by *a/B*'.[334]

In the equation n: A = a: B, where n is the value of the commodity, A – the sum of the values of all commodities, a – the price of the commodity, B – the sum of all commodities, – the relations of value mechanically oppose the relations of price. It is completely unclear what real connection exists between value and price, the sum of the values and the sum of prices, which would give the right to measure the relation of value by the relation of price.

This connection Simmel does not indicate, and cannot provide because social labour time, the real substance of both relations he does not understand.

However, trying to fill this gaping hole, Simmel finds, that 'it is sufficient that both play a part in human life, within the system of men's practical ends, for the quantitative modification of one [money] to become an index of the other [quantitative modification of goods]'.[335]

This wording is extremely vague and explains absolutely nothing.

But Simmel has to overcome one further difficulty. Usually, under relative measurement of two magnitudes by order of proportional connection with the other two, qualitatively different from the first two, magnitudes, the latter appear as constant, for *the given case* fully determined magnitudes.

In the expression n : A = a: B, that is the sum of the price of all commodities has a magnitude, changing literally every minute, depending on very complex and multiple factors. This alone

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assessment of price.

To Bendixen's claim that the value of money is only reflective value, derivative of all known to us prices, subscribe with both hands also the quantity theorists.

Especially clear the connection between nominalism and quantity theory is shown in Schumpeter. Like Bendixen, Schumpeter sees the value of money or, otherwise 'the purchasing power of unit income' derived from the value of all opposing to it commodities.

'Value of money can mean nothing but the purchasing power of the income unit. This is not the same as exchange value, nor is it based on use value. At the core of the concept of purchasing power is the concept of price: purchasing power assumes price' (Schumpeter 1956, p. 165). Here is the barbaric mix of value and purchasing power of money, value and price of commodities. With the introduction of the category of money income unit Schumpeter can escape from the error of quantitative theory, as Wieser was unable to do.

In what relation stands the sum of money income unit to the sum of the price of all commodities?

'Given stationary (!) equilibrium, the money value of all consumer goods should equal the money value of all producer goods, and both identically equal the sum of all money incomes' (Schumpeter 1956, p. 153). It is easy to see that if the situation was as Schumpeter depicts, there never would be difficulty in the sale of goods, there would be no crises. Substituting a monetary by an exchange economy (and to this leads in the final light nominalism, as well as the quantity theory), Schumpeter comes to the vulgar banalities of the prince de la Science – Say.

In our opinion, Schumpeter quite correctly stresses that 'the basic idea of the quantity theory is not only compatible with the claim theory, but *actually postulates the latter as its deeper justification*, as Mill already had suggested' (Schumpeter 1956, p. 163). The consequent nominalist has to be a quantity theorist, the consequent quantity theorist – a nominalist.

[334]Simmel 2004, p. 135.

[335]Simmel 2004, p. 135.

speaks against the the assumption of the possibility of measuring the proportions of value with proportions of prices. But there is another snag.

How do A and B, the sum of the values and the sum of prices, magnitudes, empirically not recognised at all, find their reflection in the stated proportions?

Simmel also here tries to find a loophole.

The fact that we empirically do not at all imagine to ourselves the quantities A and B, is explained, according to Simmel, by the fact that changes of the sum of prices and the sum of values

> are not easily observed and we are not conscious of their function as denominators; we are exclusively interested in the numerators n and a for each individual case. Thus, the idea could emerge that n and a correspond to each other in some absolute and direct way; and if this were so they would indeed have to have some identical quality ...

The reason for this is that

> only the distinctive features of each phenomenon, the absolute individuality, enter our consciousness, while the general and fundamental elements remain unconscious. Between these two extremes, there exists at various levels those points or aspects of the total phenomenon upon which the greatest attention is focused. In general, it may be said that theoretical interests direct awareness more to generalities, practical interests more to the specific features of things.[336]

Let us agree for a moment with the reasoning of Simmel. Let us assume that the proportional measurement of the value of commodities is a mental process, mediated theoretically in the interests of our 'greatest attention' [highest consciousness]. But how in reality does this process happen, how does this reduction of the individual to the universal happen? *On this Simmel does not give a response.*

To relate some phenomenon to that which takes place beyond the threshold of our consciousness, does not yet mean to explain the phenomenon. Only a single negative feature does not go far. The Marxist theory of political economy also argues that the individual boils down into the universal beyond the threshold of human consciousness, but besides this it has an explanation of that real process, by means of which occurs the equation of the

[336]Simmel 2004, p. 135.

individual numerator units of labour expenditure to the common denominator – the empirically not perceived social labour time. The gulf drawn by Simmel between commodities and money, the measured and the measuring substance, is transferred by Simmel into human consciousness, but the announcement of the riddle of the money form of value by a psychological phenomenon still does not mean to solve this riddle.

The denial of the substantial equality of money and commodities leads Simmel to the inability to explain the historical emergence of symbolic money from commodities. Although Schumpeter also argues that 'the historical origin of the value of money lies in the value of the money commodity',[337] such a statement clearly contradicts the presuppositions of nominalism.

The enigmatic leap from commodity to money, from the qualitative amount to pure amount is transferred here from the plane of pure logic to the plane of the historical-genetic. If nominalism could safely make this jump, the riddle of the equivalent would have been disclosed. The historical evolution of money towards its replacement by symbols of money, money surrogates, could be understood only from starting from the proper representation of the mutual correlating functions of money, explained by Simmel from the point of view of marginal utility.

However, although money in its development also seeks to obtain the character of pure symbol, it does not fully achieve this, because, according to Simmel, the atom of an own material of value, embedded in money, is necessary, in view of the imperfection of our knowledge, not comprehending still the so accurate determination of the proportions, in order for a *substantial equality between the measuring and the measured to have become superfluous*.

Thus, Simmel insurgent with fire and sword against those who claim the qualitative equality of values and prices, money and commodities, has himself come, albeit in the form of minor concessions to the 'atom' of substantial value, to the negation of the ideal and abstract nature of the money unit. A more clear bankruptcy of nominalism in the conception of Simmel is found if one turns attention to his previous formula n: A = a : B. Since the total amount of the price – B, regardless of the deviations of the price units from their underlying values, is always equal to the value of the entire mass of commodities – A, then also n = a, that is the value of the commodity is its price.

Logical circle finished! In an effort to prove that money does not comprise a single atomic value, that is that prices, as the expressed ideal counting function of money[338] and the value

[337]Schumpeter 1917/18, p. 64.

[338]And precisely: to the function of account money the nominalists reduce the whole nature of money. The claim

of the commodities are incommensurable, Simmel in fact did not only arrive to the proof of commensurability, but also their identity. A wonderful illustration of our earlier assertion that the 'logical consequence of the assumptions of commodity fetishist and psychological theories of relational value is the identification of price and value'.

The problem posed by Simmel, – of how money, having no intrinsic value, can measure the value of commodities, how the transition of qualitative amount – value to a numerical amount, an abstract number – money, this problem represents the philosopher's stone, in search of which the nominalist sages inevitably become tangled in internal logical contradictions.

Let us take the case of Bendixen.

Like in Simmel, money for Bendixen does not have value. 'That what we call the value of money is only a reflective presentation, a derivative of to us all known price'.[339]

> At the same time, as the assessment of the value of one thing happens, judgments are made about its relation to all other goods. But one value is not determined by itself, but is defined by its relation to other values. Thus, the world of values is a boundless chain of value relations. For comparison of several relations it is necessary to reduce them to a common unit of account. Everyone knows how to deal with a large number of fractions with different denominators. Bring them to a common denominator.
>
> A fraction is nothing other than the relation of two magnitudes (the numerator and the denominator). Just as by bringing to a common denominator solves the relation of numerators to different denominators and the numerators emerge into a new relation with the common denominator, so also the values are detached from their relations to each other and brought to a common denominator, allowing mutual comparison of an unlimited number of values. This work is done by money ...
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> Money is the common denominator of all values.[340]

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of Katzenelenbaum as if the 'abstract-nominalist direction boils down the essence of money to its function of *measure the value* and dissolves to this function all the others' (Katzenelenbaum 1921, vol. 1, p. 29.) is to us a wrong presentation if only already because the nominalist, does not realise the problem of value, erodes from price its substance value.

[339]Bendixen 1912, p. 16.

[340]Bendixen 1912, pp. 21–2. But if the value occurs as a result of psychological assesment it is not clear why there exists a 'boundless set of value relations'. After all we do not put ourselves *at the same time* in relation assessment to all objects. The psychological point of view on the evaluation of the value of commodities, professed by nearly all members of nominalism without exception, advertised by them as the product of modern Western thought, in fact returns us to the medieval metaphysics of illusionism. Does not the view of nominalists on the assessment of value remind of the proclamations of Berkeley and Hume, does it not lead to the Cartesian 'cogito ergo sum'? This illusionism, driven in Hume toward solipsism, to the dissolving of all the outside world to the 'I', like also the illusionism of value of nominalism, stands in clear contradiction with the world, objectively existing regardless of our perceptions, with prices, objectively existing, regardless of how our

The analogy with the reduction of fractions to a common denominator does not hold water. First of all, it is entirely unclear how the value denominators in value relations transform in denominators of money. If we take the reduction of fractions to a common denominator then in fact both the common denominator and all the other denominators are *commensurable*, because they all express a determined sum of abstract numerical units.

But in what is expressed the commensurability of value denominators and the common money denominator? On the contrary – the money denominator – for Bendixen – does not contain a single atom of value, it is an *abstract number*; the value denominator expresses a known qualitative, and not an abstract number. On the other hand – common denominator is comparable with all the new numerators, formed by bringing the fractions to a common denominator, because they are all different amounts of the same substance, number. This is not necessary to assert, however, with respect to the money denominator, because, in the opinion of Bendixen, its substance is number, while the substance of the value numerator is value.

How artificial and contrary to reality the substantial separation is of money from commodities, is shown by the fact that in another article 'Vom Gelde als Generalnenner' ('On money as a common denominator') Bendixen actually abandons his assumption and comes to the recognition of the substantial unity of money and commodity.

> Imagine to yourself that money as means of payment and unit of value has disappeared, and all values are expressed in their relation to other values – one is allowed to conceive this, although it hardly could really happen. Then we would get an unlimited number of relations or fractions with different denominators. One person gives an estimate of her dress in boots (D/B = 5/1), another in annual salary (D/AS = 1/7 = 0.143/1). In these cases the value denominator for the value numerator – dresses, is in the first case – boots, in the second – salary. Similarly, a farmer can express the value of horses in pigs or calves and vice versa. But all these relations are not comparable with each other until they are brought to a common denominator and the latter is used for the expression of the value of all other commodities. Then one can take a metal, for example, silver, and express the value of commodities in a weight of this metal. The numerator of dress discards the denominator boots and takes as a denominator 1 pound silver (D/lb ratio = 2/1); boots, in value constituting 2/5 lb

'assessing thought' (*der werfende Gedanke*) relates to them.

> silver, give such a relation: B/pounds. ratio = 0.4/1; the horse relates to the 1 lb silver as 10:1, pigs as 3:1 and so on. In this way, using a common denominator – 1 lb silver – the value of all commodities are brought in connection with each other and thus is given a proportional number (2:0.4:10:3) denoting the relation of values of the numerators to a common denominator – pound of silver, which, as unit of value, is the number of 1.[341]

The fundamental error in the reasoning of Bendixen is that 1 lb silver is not a common denominator, but the generally accepted unit, the *universal equivalent*. This unit is only the necessary *prerequisite* for the common denominator. This is evident from the following considerations: the relation to 1 lb silver is determined; for boots as 2:5, for horses as 10:1, for pigs as 3:1; we get thus the fraction: 2/5, 10/1, and 3/1. Bringing them to a common denominator 5, we get: 2/5, 50/5, 15/5; the relation of these numbers will correspond [as] 50:15:2. The resulting numbers in Bendixen: 2:0.4:10:3 are still not brought to a common denominator, because among them there is a decimal fraction. The unit of value – 1 lb silver – is formed here not by the number 1, but the number 2.

The above example of Bendixen has shown well, how with the development of relations of exchange from the accidental and simple form value the expanded and universal form of value emerges; but the logical leap from value denominator to abstract denominator he failed to manage, because 1 lb Silver is not an abstract, but qualitative number. In the given citation Bendixen has disproved himself: he showed that the money is not at all a common denominator, that firstly, 'it is not money that renders the commodities commensurable',[342] and secondly that money is not an abstract but a qualitative number.

Based on the denial of the substantial value of money, Bendixen endeavours to prove that changes in the prices of commodities can lie on the side of commodities only, but not money. If the 'value' of money is only a reflection of the reflecting value of the commodities, then for business calculations this or other height of price level is indifferent.

> For business life this phenomenon (change in prices. – G.D.) does not exist. Rising or falling value of money is only important for monetary credit operations and fluctuating interest rates reflect fluctuations of money prices… The changing purchasing power of money is only the object of theoretical studies, but not business

[341]Bendixen 1920; article 'Vom Geld als Generalnenner', pp. 26–7.
[342]Marx 1976, p. 188.

calculations.[343]

Recent facts from the war and post-war era convincingly shatter the arguments of Bendixen. It was exactly in Germany in the era of the rapid fall of the German Mark that the purchasing power of money was not only an object of theoretical research, but also an object of the most prosaic business calculations. All the speculation on the fall and rise of the rate of the Mark, all concluding trade deals precisely also had for speculative object the changing purchasing power of money.

And in currency dumping, which gave the possibility of German industry, in spite of the general crisis of the economy, in spite of the heavy plight of the broad masses, to work with a full load on the world market, – had this currency dumping really meaning only for lending operations, was it indifferent for industrial capital?

The facts contradict all those conclusions that lead Bendixen to deny the substantial value of money.

Over the problem of equivalent unsuccessfully fights also another prominent representative of modern nominalism – Karl Elster.

For Elster the unit of value is an amount, a number; money is also a number,[344] but at the same time also 'the ability to participate in the social product'.[345] But the one contradicts the other thing, as 'participation unit' (*Beteiligungseinheit*) is not a pure number, but a qualitatively determined actual unit.

To this comes, however, also Elster himself: 'A unit of value is a quantity, a number; but the possibility of participation is a substance, quantitatively expressed through the unit of value'.[346]

Here Elster runs into a clear contradiction: money is at once a pure and substantial number! Trying to break the vicious circle of internal contradictions, Elster in the end absolutely abdicates from the search for a connection between commodities and money.

The problem of price-formation, the problem of the growing in of the subjective in the objective is declared unfathomable. 'From values, as subjective perception there is no bridge to prices, as objective numerical expression'.

Such a statement – essentially – denotes the recognition of the full bankruptcy of the theory of nominalism before the mystery of the equivalent form of value.

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[343]Bendixen 1912, p. 28.
[344]Elster 1920, p. 46.
[345]Elster 1920, p. 86.
[346]Elster 1920, p. 95.

Before proceeding to the statement of the problem of the value of money in the system of Knapp, one should ask the question: whether this system in general is a subject of *economic* analysis?

Such a question, perhaps, may have seemed vacuous, if we would not have with us the widespread understanding about the conception of Knapp, as a purely legal, juridical construction. There could be nothing of economic phenomena, of theoretical economy in common with this conception. This is the widespread opinion, to which adjoin most critics of Knapp – the metallists, the Marxists and even some nominalists. With a light hand Mises divides all theory in catallaxy and acatallaxy, that is, theory dealing with phenomena of exchange, and theory completely ignoring the latter and built on pure-philosophical, legal, ethical, and so on premises; for the theory of Knapp the name acatallactic is firmly established. The nominalist Liefmann speaks about the work of Knapp as an 'absolutely not economic, pure-legal structure'.[347]

In another place we find in him the following – unflattering – characterisation of the Knappian system; 'Knapp's ideas are not economic theory, they are nothing but a false (*falsch*), that is *merely* legally validated confirmation of correct inductive and historical observations'.[348]

With no less force also Block pounces on Knapp, criticised in his book on Marx's theory of money. 'The state theory of money is a juridical and historico-legal, but not economic theory. It appears at least from this that the doctrine of the validity (*Geltung*) of money took the central place in Knappian study, while the central problem of economic theory of money – the value of money Knapp completely ignored'.[349]

Another author, a Soviet scholar, totally denies to the theory of Knapp any connection with nominalism and offers to see it apart from economic nominalistic theories, as a theory purely of law.

> The economic formulation in Knapp is so helpless that it can hardly claim serious scientific meaning, in addition tallies little with his whole system ... *This obliges us to*

[347]Liefmann 1916, p. 25.

[348]Liefmann 1916, p. 19.

[349]Block 1926, p. 62. The critique of the Marxist theory of money in Block is based on the following argument: in the theory of money of Marx two theories of money must be distinguished: the first – philosophical-social – should be completely rejected, because 'economic categories cannot include philosophical content'; the second – an economic theory of money. Thus Block's position is the diametrically opposite position of Franz Petry, who, likewise distinguishing in Marx's theory two strings, considered as correct, not the economic, but the social-philosophical theory of Marx.

The objections of both critics (their point of view closely recalls the views of Struve, Stoltzmann, and so on, also seeing in Marx two theories), of course, are wide of the mark, since their main premise – the artificial division of the real unity of social forms and the material process of production – is at bottom false.

> *recognise that in Knapp there is no theory of nominalism*. His rightly called state theory, is a system of means of payment in general and the most important of them is money, particularly, from the perspective of the state, the comprehensive determination of the dependence between the development of payment transactions and the state.[350]

If the case was rightly put by the above named authors (to some extent also Hilferding), then attempts to subject Knapp's system to critical analysis, we would need to completely abandon. You can only criticise there, where there is common ground. Inasmuch as Knapp's theory recognises only juridical, dogmatically legal significance, insofar also the criticism of this theory is only possible on the basis of law, and there the economist has nothing to do. Knapp's system should be equated to the system of Stammler, and subjected to fire from the heights of the general sociological standpoint of dialectical materialism, dissociating itself in this way from the field of study of Marx's theoretical economics.

This interpretation of Knapp's theory seems to us deeply wrong, and based largely on misunderstanding. Partly guilty of this is also Knapp himself, who sticks out in every way the legal nature of his vision and at every step distantiates himself from the annoying proclivities of market forces. This does not hinder, however, that the economic element, ousted by Knapp at the door, unbeknownst to him burst through the window – and this is due to the *internal inconsistency* of Knapp's system, the vicious circle, in which the notorious 'iron logic' of the creator of the theory of the state money hopelessly is entangled.[351]

In this case what interests us is not that the theory of Knapp is a *state* theory of money, but that it is what is called a *nominalist* theory of money. The emphasis on the rule of law and the state is not essential for nominalism. On the contrary, in this respect, Knapp is closer not to the Austrian, but to the *historical* school. Theories of Bruno Hildebrand, Diehl, partly Ludwig Stephinger and others suggest that, based on the historical-legal point of view, you can arrive – consequently or eclectically – to the recognition of the substantial value of money.

In Knapp's book the economist is not interested in the teaching on *valor impositus*, rooted in the dark Middle Ages, but the doctrine about the nominal unit of value. Therein just also lies the peculiarity of the state theory of money, that Knapp throws on himself a chartal cloak in

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[350]Ugarov 1925, p. 286.

[351]Elster fully justified stresses, that already the very notion of payment and means of payment, on which the state theory of money is based – already these conceptions, leaving aside the impact which the state has on the financial system, have not only a dogmatic-juridical content, but include in themselves highly important economic problems (Elster 1920, pp. 2, 3).

order to sing serenades under the windows of the nominalists. Chartalism is used here to cover a logical confusion, resulting from the inability of nominalism to solve the mystery of the equivalent.

We are not interested in this case in the question whether Knapp put *consciously* before himself this puzzle, whether he was trying to resolve or just *escape* from it; important is that the thought of Knapp moves in the orbit of the same contradictions with the antithesis of money versus commodity, in which the thought of Simmel, Bendixen and Elster moves.

From this precise point of view we also attempt – out of necessity very briefly – to cast a retrospective glance on the construction of Knapp.

Again, I emphasise: from the fact that Knapp's theory of value of money is not developed, not emphasised, it does not at all follow that he has completely no theory of value of money.

> The theory of the value of money is constructed *subconsciously*; it is not made explicit; it is not completely thought out. For if it were consistently thought out to its logical conclusions, it would become obvious that it is self-contradictory.[352]

* * *

Already in the first chapter, Knapp faces a difficult task: how did the transition occur from real pensatory[353] means of payment that circulated in exchange back in the early stages of human history, to the developed ideal means of payment, money; how to make the leap from qualitative amount to pure amount, number?

We have already mentioned, that for nominalism this problem is unsolvable, because the puzzling somersault from commodity to money, under which nominalism smashes to pieces its forehead, is not eliminated but only transferred from the pure-logical sphere into the historico-genetic sphere.

Arguing that tender in its historical genesis is the exchange of goods and owes its origin to the domain of exchange,[354] Knapp in the very first pages had to fall in clear contradiction with himself. The circulatory property;[355] the constitutive conception of means of payment,[356] just recognised by the institute of social exchange, Knapp has transformed already in its

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[352]Mises 1953, p. 464.

[353]Its purchasing power is determined by weighing. [Bortkiewicz (1906) notes that Knapp's terminology does not add any explanatory power. See also Bortkiewicz 1918a.]

[354]'General exchange-commodity is ... an institution of social intercourse; it is a commodity which has obtained a special use in society, first by custom, then by law'. (Knapp 1924, p. 3). Thus, for rule of law here is recognised only the second, sanctioning meaning.

[355]The use of means of payment for production payment.

[356]'A means of payment is ... a movable object which can in any case (*Jedenfalls*) be used for circulation' (Knapp 1924, p. 7).

historical genesis – in a phenomenon of the rule of law.[357] It follows, tender is a phenomenon of the rule of law.

So, pensatory tender, the most ancient and primitive form of tender, in Knapp – at one and the same time is exchange of goods – a phenomenon of social life, a system of real units of value and a phenomenon of the rule of law, a system of abstract accounting units, decreed by the state.

In order to cover up this gaping contradiction in the definition of the basic concept of his system – the concept of means of payment and to obscure the transition from real to nominal units of value, that nominalism cannot afford to explain, Knapp is forced to secretly erase from the concept of means of payment the for it circulating commodities, to oppose to it the exchange of commodities. This is achieved at the expense, that the non-pensatory, and also the more advanced means of payment – money – are dissolved in the concept of rule of law, the exchange of goods and the hidden in it commodity trade unnoticedly for the reader are detached from means of payment, with which it still on page three was integrated.

Instead of commodity exchange steps forth debt, the real unit of value is replaced by a nominal one.

Means of payment are declared means of repayment of debts. But, debts emerge in the result of economic exchange, that is, in the result of the movement of commodities. Means of payment, as mouthpiece of debt obligation, only therefore also can be read per units of value, because commodities still before the conclusion of a credit transaction were equated to means of payment, expressed in units of value. Thus, Knapp again encounters the cursed question – *mene tekel peres* of nominalism – the problem of expressing the value of commodities with the value of money and escapes out of this trap only, cleverly sweeping the tracks, by replacing the economic circulation of commodities with the legal fiction of duty, as a purely legal concept, involving the concept of state and the amphitropy[358] of the members

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[357]'The use in exchange is a legal phenomenon, therefore, *even autometallism is a legal form of means of payment*' (Knapp 1924, p. 7).

[358]The statement about amphitropy, that is about a constant *ratio* of debt obligations during the transition to the new unit of value, on which Knapp bases the rating [nominality] of lytric debt and unit of values, seems to us incorrect for the following reasons: a) Introducing new units of value, the state *directly* does not decree new monetary value of payments liabilities, the magnitude of the latter in units of new value determines the reflective changes in the prices of commodities. That is why the adaptation to the new money units of payment obligations are always performed with a delay and unevenly, by virtue of which the former ratio of lytric debt is violated. b) It is wrong that each member of payment exchange should be considered simultaneously as both debtor and creditor. In the process of historical development entire classes and class factions get into the position of permanent debtors, others in the position of permanent lenders.

The state usually acts as an advocate or opponent of one or other social group and seeks the introduction of a new money unit not to support amphitropy, but to undermine it and greatly alter the ratio of payment obligations (the English money reform in the late seventeenth century, which went to the benefit of the young British bourgeoisie, acting as the creditor of the government, war and postwar inflation, and so on).

The desire of Knapp to put the state forward, as some construction above classes, whose supreme task is

of the payment organisation.

Thus, in contradiction with the earlier advanced position on the socio-economic nature of the means of payment, Knapp is forced, in order to cover up the logical leap from real to nominal unit of value, to avow that the development of means of payment is done in the bowels of the rule of law, the nominality of the money unit,[359] the state, debt, the means of payment – in essence are logical categories.

Thus, Knapp is forced to dissolve the means of payment in money, which leads him as a result to the clear absurdity: money exists even before it has emerged, because, if the means of payment under autometallism[360] is a phenomenon of the rule of law, if the unit of value also here is nominal, if it is proclaimed by the state, then what is its difference from chartal[361] means of payment, that is, from money?

It is clear that here in Knapp the ends do not meet. Recognition of a nominal unit of value also under autometallism *upsets the whole genetic scheme of Knapp*. In addition to the contradiction with the determination of the circulatory property and means of payment, the failure of nominalism to resolve the problem of the value of money entails Knapp in a vicious circle in the determination of the relationship between means of payment and units of value. There are three definitions of means of payment in Knapp:

1) 'A means of payment is ... a movable object which can in any case (*Jedenfalls*) be used for circulation' (p. 7). A thinly disguised tautology! What does it signify to be used for circulation? This signifies to be used as a means of payment.

2) 'A means of payment is ... a movable thing which has the legal property of being the bearer of units of value' (p. 7). Again in this definition, the concept of unit of value. But what is the unit of value? 'The unit of value is nothing but the unit in which the amount of the payment is expressed' (p. 8). So, a great vicious circle! Means of payment is derived from unit of value, and the unit of value from the means of payment.

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preserving the integrity of payments exchange, characterises him as an apologist for the bourgeoisie, seeking to conceal the class character of the state. Equally wrong is also the statement of Knapp, as if the creator of the nominal unit of value, the force, turning amorphous pensatory means in formed chartal – money, was the state. The history of money circulation shows that before the state acted as a body proclaiming a determined value of coins, their shape, etc., this pleasant duty took upon itself (yes also now is taken in some countries, for example, in China) any organisation, directly arising from the economic exchange, any private person who enjoyed authority on the market (see Babelon 1897, pp. 95, 96 and elsewhere; Helfferich 1923, p. 39). Government intervention does not help Knapp to make the logical leap from a real to a nominal unit of value, from money – commodity to money – symbol. To present the state as a force that created money, is the same as to explain the creation of the world – with god.

[359]"The nominality of the unit of value, and therefore of lytric debts ... will exist *for ever*. It is compatible with *any* form of the means of payments' (emphasis mine. – G. D.), Knapp 1924, p. 19.

[360]Autometallism – to Knapp is a system of payment, when metal functions in the quality of means of payment.

[361]From the word charta – sign, which usually means a document, the power of which does not depend on the material, which served for its manufacture. [Bortkiewicz (1918b) stressed that apologists of paper money vulgarise Knapp's chartalism, since for Knapp *any* money is chartal.]

3) Finally, on page 152 we find an indication that for the conception of means of payment 'does not require the actual delivery of pieces, but a legal transfer of claims and counter-claims in units of value directed to a Central (Clearing) Office'. Not to mention the inaccuracy of this definition in essence,[362] here again the constitutive moment is the nominality of units of value, which in turn, are deduced from means of payment.

Thus, the sphinx of the equivalent form of value, the riddle which Knapp proved unable to solve, took revenge – and took revenge brutally already in the first chapter in the following points:

a) contradiction in the determination of circulatory property;
b) contradiction in the determination of means of payment;
c) vicious circle in the determination of the inter-relationship of means of payment and nominal units of value.

In the outlined contradictions, due to lack of understanding of money and commodities, is in nuce the whole contradiction of Knapp's system, deployed also further in the construction of the genetic and functional schemes.

For lack of space we cannot enter into detailed review of both schemes in terms of the development of the basic contradictions, arising from the nominalist conception of the problem of money in Knapp.

We note only that the attempt of Knapp with cash money – the primary link in the development of chartal means of payment – to throw a bridge from the real unit of value to the nominal ends in failure. There is no transition from pensatory to chartal tender in Knapp.

As concerns the functional scheme, the scheme, characterising the *modern* constitution of means of payment, then, the effort all the same, regardless of the many contradictions, showing that money – is created by the rule of law, that its essence is a nominal unit of value, Knapp with the first thing throws overboard the for him uncomfortable ballast – accessory money.[363]

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[362]For the following reasons: a) The essence of the payment consists not of juridical transfer of claims, but precisely a physical transfer of things: Knapp makes here the same mistake as in Schumpeter, imagining to himself money as an accounting system, comptabilité sociale, b) Under this definition does not fall money, circulating simultaneously in two or more states – in Knapp's terminology – synchartal money [for example the Latin Monetary Union].

[363]All types of money, that the state does not impose on a recipient in their payments and that a recipient cannot claim exclusively. It is typical that at the basis of the functional scheme (which Knapp artificially seals off with a Chinese wall from the genetic scheme) lie only centric payments [see Knapp 1924, p. 96], that is payments, in which one of the subjects is the state.

The elimination of paracentric payments as 'regulating themselves' (!) (what then can be the connection between nominal unit of value and private obligations?) is typical for Knapp. Not being able to solve the mystery of the equivalent, Knapp is forced to lock himself in the circle of organised state economy, [to close himself off] from real payment relations, behind which hides the circulation of commodities, from the world of prices and market relations, [that are] disastrous for nominalism; Knapp is forced, like an ostrich, to bury his

Accessory money is recognised as commodity.

But since money cannot have value,[364] since it cannot be a commodity,[365] then, being consistent, Knapp would have to deny accessory money, as money, that is, to go to the destruction of the functional scheme. There remains the last stronghold, – valuta money,[366] in which, as in a focus, concentrate all the nominalist rays of Knapp's system. According to Knapp, valuta money, as opposed to accessory money, can have neither agio, nor disagio, cannot be a commodity, cannot have value.[367]

But how can you talk about measuring the value of accessory money valuta, if the latter does not posses value? Knapp himself falls into clear contradiction, recognising that the silver guilders were *less valuable* than paper guilders (the onetime then in Austria valuta money).[368]

If silver guilders were less valuable than paper, then paper was more valuable than silver. But how can one say that the paper guilders – valuta money – is more valuable than silver, denying to it the property of value?

In the same contradiction Knapp runs, dividing the transitions to new valuta money in rising (*steigend*) and falling (*sinkend*).[369] The concepts of 'rising' and 'falling' suggests a comparison of the old currency money, become now commodity, and new ones, being in the opinion of Knapp, a system of abstract counting units. The comparison of old and new valuta money, gives Knapp the possibility to assert that the new valuta money is higher or lower than the old, to assume the substantial equality of both types of money. One could have pointed out one more contradiction in the formulation of Knapp: for example, in the chapters about choosing valuta money, the transition to new valuta money and so on, Knapp actually rotates inside a *vicious circle* – the nominal unit of value is derived from price, already read at nominal unit of value.[370]

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head in the sand of a dry formal scholastic scheme, substituting the unorganised by the organised economy, and circulation by exchange, in its logical development leading to the idea of a moneyless economy, to the idea of world kontokorrent accounting [current accounts].

[364]Knapp 1924, p. 30.

[365]Knapp 1924, p. 155.

[366]Money that the state imposes for its payments and which the recipient may demand. ['The definitive kind of money which the State chooses as final for its own payments and makes compuIsory in dubious cases, is called valuta money. All other kinds of money are called accessory. The valuta money is the "standard," in the narrower sense of the word' (Knapp 1924, p. xii).]

[367]Knapp 1924, p. 162.

[368]Knapp 1924, p. 163.

[369][Knapp 1924, pp. 194–5.]

[370]Knapp himself acknowledges that an obstructional transition to new valuta, that is a transition, causing a 'piling up' (*stanung*) of state offices with accessory money – is the most common (*allergewöhnlichste*) transition. This phenomenon of *stanung* of accessory money, caused by the market, by pantological moments, depends on price. So, the fate of valuta money, and therefore also the fate of the nominal unit of value, depends on price, the same price, in its turn, is stated by the nominal unit of value.

The main pivot of all above mentioned contradictions, stated – of necessity – very briefly and concisely – is the denial of the substantial unity of money and commodity, the denial of the value of money, as a property, immanent to the very nature of the money commodity.

Chapter Twenty

Credit Romanticism in Golden Fetters (April 1931)

Zachary Atlas[371]

1. The credit and monetary system

This article is devoted to the critique of the chief representatives of the modern bourgeois-apologetic school of *credit romanticist expansionists*. Credit romanticists they are because, like Law and Péreire they see in credit an unlimited driving force of production and a powerful means of solving the basic contradictions of capitalism. *Expansionists* of credit they are because with continuous expansion of credit, with unlimited credit creation the road 'opens' to the realisation of their credit-romanticist ideas. Just like old John Law 'stunned the world' in the eighteenth century with his 'extravagant' ideas and 'experiments' in the field of credit creation.

But the twentieth century is not the eighteenth century, and that is why Hahn is not simply Law, Schumpeter – is not MacLeod and Silvio Gesell – is not Proudhon or Saint-Simon. Between the old and the modern bourgeois and petty-bourgeois credit romanticists there is a significant difference.

Credit romanticism emerged at the dawn of industrial capitalism, bloomed in the initial period of its development, yet represented during the whole second half of the nineteenth century nothing more than an episodic phenomenon. Again it has revived in all countries in the period of the general crisis of capitalism, in the epoch of the decay of capitalism and proletarian revolutions. The bourgeoisie and its ideologues is trying to resurrect any and all ideas, which could show that there are still hidden forces able of fertilising with creative energy, with the greatest life impulses a capitalist system, torn apart by internal contradictions, showcasing its impotent attempt to escape from them, and standing under the terrible blows of the 'final, decisive' class battles.

Marx gave a comprehensive description of the old credit romanticists. He pointed out the dual character, immanent to the credit system, namely, 'on the one hand, to develop the

[371][After the second world war Atlas (1903–77) was considered 'the most eminent of Soviet monetary economists' (Jasny). Most significant seem to be his early articles, for example his attempt towards a Marxist theory of bank credit (Atlas 1929). In his critique of Hilferding's theory of money, he stressed the radical revisionism of Hilferding's anti-Marxist theory, its reformist ('social-fascist') politics, and Kautsky's inability to criticise it based on a proper understanding of Marx's theory of the commodity (Atlas 1931a). Atlas wrote the textbook *Money and credit* (1930).]

motive of capitalist production, enrichment by the exploitation of others' labour, into the purest and most colossal system of gambling and swindling, and to restrict ever more the already small number of exploiters of social wealth; on the other hand, to constitute the form of transition towards a new mode of production. It is this dual character that gives the principal spokesmen for credit, from Law through to Isaac Péreire, their nicely mixed character of swindler and prophet'.[372]

This characterisation does not apply to the modern credit romanticists. One cannot call them 'prophets', because as 'motive of capitalist production' credit already fully exhausted itself, and the transitional form to a new mode of production in the USSR became a fact, known to millions around the whole globe. Modern credit-romanticists – are not 'spokesmen for credit', not prophets, but they really are '*swindlers*', though in a somewhat different sense than this has been said by Marx about Law and Péreire. They are 'swindlers' in theory, because *they themselves do not believe in that which they say, because, overflowing with romanticism in theory, they turn their back to it in practice*. Law, Péreire, Saint-Simon were consistent, from beginning to end. They did not create theories alone: their theories were *concrete plans, economic and social programs*, which they sought to implement in practice. Another thing is the credit romanticism of the twentieth century. In theory – a 'golden age of capitalism'; in practice, provisions and provisos, depriving this theory of all practical sense. Their theories, no matter how filtrated, logically-refined they are (Schumpeter), with whatever pseudo-scientific apparatus of new concepts they are enriched (Hahn, Sombart), are helpless in scientifically related work, representing by themselves only ideological weapons in the hands of the bourgeoisie. *Modern credit romanticism – this is one of the methods of the apology of capitalism*. Precisely in the apology of capitalism, in proving the vitality of the capitalist system lies the main practical sense of all works of modern credit romanticists from *Hahn* and *Schumpeter* to *Gesell*, *Feder* and *Değmer*.[373]

True, with American credit-partisans there is an element also of actual practicality, which consists in the point that under the flag of a general idea is implemented in fact, through the Federal Reserve System, a control and pressure of large-concentrated finance capital over

[372]Marx 1981, pp. 572–3. [This was quoted again by Atlas in an article written together with Matyukhin on the eve of the end of dollar convertibility (1971). Atlas was the doctoral advisor of Matyukhin. Their article responded to the negative view (held for example by Milton Friedman) about the role of gold as money in modern capitalism. It concluded that gold in its function of world money must not be regarded in isolation from its other functions, from which it arises as money. Gold is the money commodity and therefore still is the genuine world money. Matyukhin later wrote several books on money and credit where he no longer defended this position. In some works he briefly commented on the gold debate in *Die Neue Zeit* (Matyukhin 1977, 1984). He later became the first chairman of the Russian central bank.]

[373][Lucien Albert Hahn (1889–1968). 'Free-money'-theorist Silvio Gesell (1862–1930). Nazi economist Gottfried Feder (1883–1941). Şefik Değmer (1887–1958) was the general secretary of the Communist Party of Turkey (see anthology 1977).]

small enterprises and, on the other hand, full adaptation of the credit policy of the banknote-emission system to the needs of finance capital. Similar motives partly hide also behind the Hahnist theory. But for us the root and social background of the theory is not key, [at least] not here. That which characterises the modern credit romanticists, that which differentiates them sharply from the old romanticists, is their *half-heartedness, hesitancy*. They seem to be afraid that their theory is taken seriously by those who possess the right to open the ambit of credit creation, credit expansion, unrestricted credit inflation. Therefore, not ashamed in theory to paint a picture of capitalist prosperity on the basis of credit inflation, they in practice come to claim a golden limit to this expansion. Each of them in their own way deals in credit romanticism, and in their own way debunks it essentially in concrete conclusions, as *practical nonsense*. Hence the *profound conflict of theory and practice*. The concrete credit-policy and credit-organisational problems are solved by the bourgeoisie not on the basis of, but *against* the prevailing credit theory, and such a one appears precisely the expansionist theory. This also is the complete degeneration of bourgeois economy, as a science, the ultimate degree of its vulgarisation; the prevailing theory and the practice of the bourgeoisie turn out to be at different poles. Practice deprived of scientific character, reality hollowed from theory, it is abstracted from reality. 'Science' turned into a pure sport, into a competition over most sophistication in proofs 'within the frame of theory' of paths and methods of unlimited credit and production expansion.

It is not so much necessary to criticise modern credit romanticists, as to *expose* their duplicity, halfheartedness, in essence – *theoretical swindle*.

Werner Sombart in volume three of *Modern capitalism* claims, that 'the most interesting part of the credit problem is the question about the limits of credit, that is the question in which degree can credit be expanded without there arising disorder in the social structure of the economy'.[374] However this is not only 'the most interesting', but also the central, fundamental and general question of the credit problem. In the epoch of *finance capitalism* this question goes beyond the frame of narrowly–credit problems. *In the bourgeois literature of our days to these questions entirely is bound the general problem of the fate of capitalism*. Precisely to credit is attached the meaning of powerful, sometimes *fundamental*, factor of stabilisation and organisation of capitalism.[375]

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[374]Sombart 1927, p. 179.

[375]The idea of credit regulation of the industrial cycle in recent times is developed and promoted in England by the so called 'Cambridge school of economists'. T. E. Gregory in the journal *Economica* (1924) formulated the basic principles of this school of which we mention the following three principles: 1) Stabilization is to be attained by watching credit-creation rather than currency-creation; 2) control of credit enables short-run as well as long-run stabilization to be achieved. That is, the trade cycle is controllable at will, through credit control, even if the trade cycle is not caused by the manipulation of credit; 3) the appropriate instrument of

The problem of the boundaries or limits of credit is directly connected to the doctrine about 'organised capitalism'. This connection follows from one or other conception of the nature and role of credit in capitalism. One can understand credit either as super-historical category, or, as 'immanent' form of the capitalist mode of production.[376] From this latter point of view credit in its development is conditioned and *limited* by the patterns [*zakonomernost*: law-governed, regularity] of capitalism and cannot go beyond the *contradictions* inherent to the latter.

But this Marxist viewpoint opposes the bourgeois conception of credit. From the point of view of the latter credit, as form of economic connection, is not at all necessarily limited by the contradictions of capitalism. On the contrary, credit 'removes', eliminates the contradictions of capitalism precisely because there is no *organic* connection of credit with the latter. Bourgeois economists usually 'open' the limits of credit with *production 'in general', with productive forces irrespective of their social form. And as the productive forces 'in general' can develop unrestrictedly, then also credit expansion has not any specific-social limits*.

Hence – *credit romanticism*: – unlimited credit expansion, exempt from the 'conventions' and 'prejudices' of the monetary system, opens up unlimited possibilities for the development of production forces. If between the latter and credit expansion there really exists a straight, vulgar-mechanically understood connection, then it is easy to arrive at very optimistic conclusions. Thus, for example, such 'trumpery' measure, as the removal of legal restrictions to the emission [that is issuance] of banknotes by the central banks of capitalist countries, opens up, from this point of view, the capability of unlimited credit expansion and, consequently, an unlimited development of productive forces, or as the expansionists express it, provides the capability to 'maintain an eternally high economic-cycle'. With the help of this central regulation of credit expansion both the price and volume of production of separate branches can be regulated and, thus, not only be achieved a general and continuous upsurge of production, but also *proportionality in the growth of its individual branches*.

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control is the central bank of a given country, the appropriate methods being the use of the bank rate of discount, supplemented or reinforced by open market operations. In application this method should be orientated not only on the condition of bank reserves and exchange courses, but also by indicators (of commodity prices, unemployment, state of production, movement of foreign trade, etc.). On this platform stands, as Gregory notes, a significant group of economists. In what degree the ideas of the Cambridge school are real, the example of *America* shows. Under the presence of the Federal Reserve system in the USA at the end of 1929 bursts a grandiose crisis. And this, regardless of the fact that the Federal Reserve Board had a fine-tuned apparatus of economic-cycle supervision. But all the economic-cycle barometers let down the American stabilisers. This could not be otherwise: the so called 'social indicators' of the Cambridge school record already *accomplished* phenomena and give a signal to the central bank about a change of credit policy in order to keep safe its gold reserve and prevent bankruptcy, but *not in order to* 'stabilise the economic-cycle'.

[376]Marx 1981, p. 742.

Hence, of course, credit appears also a radical means against unemployment, as *Bellerby* (1926) believes.

Thus, credit illusions follow directly from a decidedly bourgeois, vulgar and apologetic conception of the essence of credit and the bounds of credit expansion. As soon as credit is considered outside its necessary connection with the specific capitalist conditions of productions, illusions arise of unlimited expansion of credit, 'credit creation' and the stabilisation of capitalism on the basis of the supreme and infinite development of productive forces.

To break these illusions, one must strike at the theoretical roots of this conception. It is necessary to prove that this understanding of the essence and limits of credit is wrong, that this conception suffers internal contradictions, the exposing of which by example of the most powerful representatives of this tendency also constitutes the task of this essay.

* * *

'Credit economy' – according to the well-known scheme of stages of economic development of *Bruno Hildebrand* [1864] – is opposed to the system of 'money economy'. For Hildebrand, 'credit economy' relates to 'money economy' as 'money economy' does to 'natural economy'. These are the three main historical economic systems. Thus, from the point of view of this theory, 'credit economy' *qualitatively* is different from 'money economy', it represents a completely new type of economic connections. About 'credit economy' Hildebrand spoke, as about the economy of the *future* and linked his social illusions with this system of economy. However now in the epoch of *finance capitalism*, credit relations, indeed, acquired universality, and in spite of this, the Hildebrandian utopia remained utopia. Even more than this: the contradictions, inherent in the capitalist economy, in the epoch of the highest development of credit and penetration of credit relations in all pores of the economic system, are even more exacerbated. *Credit is developing on the basis of money, and capitalism, contrary to the illusions of Hildebrand, with conservation of private property over the means of production, cannot be emancipated from this basis.*

However relatively small the gold foundation is of the credit system, it all the same is precisely the *foundation* without which cannot be erected the multi-story building of the credit system. That is why the technique of study is methodologically absolutely false, which is used by Hahn in his *Economic theory of bank credit*.

He abstracts from money, and builds, so to speak, the 'working hypothesis' of a '*moneyless economy*'. Precisely this hypothesis helps Hahn to arrive to conclusions about an unlimited,

creative role of credit expansion. Hawtrey likewise uses the hypothesis of a 'credit moneyless economy', building an abstract system of 'credit without money' [in English in original].
The methodology of *Hahn* and *Hawtrey* is as false as the counter-position by *Hildebrand* of a system of 'money economy' to a system of 'credit economy'. *Hawtrey and Hahn abstract from the very basis, from the very existential element of that system of economy which they analyse*. That is why this abstraction is empty and methodologically false, and already for that reason alone, their whole logical construction collapses, like not having a solid basis.
The credit system very widely *spreads* the frames of the money, monetary system, but this framework itself it does not destroy.

> The monetary system, – Marx says, – is essentially Catholic, the credit system essentially Protestant. 'The Scotch hate gold.' As paper, the monetary existence of commodities has a purely social existence. It is *faith* that brings salvation. Faith in money-value as the immanent spirit of commodities, faith in the mode of production and its predestined disposition, faith in the individual agents of production as mere personifications of self-valorizing capital. *But the credit system is no more emancipated from the monetary system as its basis than Protestantism is from the foundations of Catholicism*.[377]

This brilliant comparison of the monetary system with Catholicism, and the credit system – with Protestantism has a profound scientific base, which is given with the whole of Marx's analysis of capitalism. Exchange economy, in whatever degree of development we see it, comprises in itself private and social production, concrete and abstract labour, a contradiction hidden already in the very commodity, in its two poles – use-value and value, – really expressed in the conflict of *commodity and money*. The credit system does not eliminate this contradiction.[378]
That is why 'money in the form of precious metal remains the foundation from which the credit system can *never* break free, by the very nature of the case'.[379] 'Never' is emphasised by Marx himself: with this Marx wanted to make more prominent his the whole illusoriness of Saint-Simonist and Proudhonist illusions of eliminating the contradictions of exchange through credit and the conversion of money into tokens, emancipated from metal. Yet Saint-

[377]Marx 1981, p. 727.
[378]"The banking system further shows, by substituting various forms of circulating credit for money, that the latter is in actual fact nothing but a special expression of the social character of labour and its products, which however, as antithetical to the basis of private production, must always present itself in the last instance as a thing, as a particular commodity alongside other commodities' (Marx 1981, pp. 742–3.).
[379]Marx 1981, p. 741.

Simonist and Proudhonist illusions are alive until these days – it is enough to point to the German 'social-prophet', of 'creation of free-money' – Silvio Gesell, and likewise the ideologue of 'organised capitalism', of 'defetishised' social relations of capitalism through means of a 'rational monetary system', the social-fascist and interventionist – Rudolf Hilferding.

Between the ideas of Proudhon–Gesell–Hilferding, on the one hand, and MacLeod–Hahn, on the other, what is common to all of these theorists, being apologists of capitalism – bourgeois or petty-bourgeois ideologues, – is to ignore the most fundamental contradictions of capitalism and not to understand the essence of credit, as 'an immanent form of the capitalist mode of production'. The social character of labour under capitalism cannot be expressed other than in a certain thing, embodying social labour, namely – in gold. Therefore an explosion of the contradictions between private-concrete and abstract social labour in the form of crisis – is *outwardly* reflected in the inability to turn commodities into money. Credit does not eliminate this contradiction, because

> credit money is itself only money in so far as it absolutely represents real money to the sum of its nominal value. Hence we get forcible measures, putting up the rate of interest, etc., in order to guarantee the conditions of convertibility to gold ... But the basis for it is provided by the basis of the mode of production itself. A devaluation of credit money would destroy all the existing relationships. The value of commodities is thus sacrificed in order to ensure the fantastic and autonomous existence of this value in money. In any event, a money-value is only guaranteed as long as money itself is guaranteed. This is why many millions' worth of commodities have to be sacrificed for a few millions in money. This is unavoidable in capitalist production, and forms one of its particular charms. In former modes of production, this does not happen, because given the narrow basis on which they move, neither credit nor credit money is able to develop.[380]

We found it necessary to fully bring out this place from *Capital* because here with classical clarity and exhaustive completeness is elucidated the relation of credit money created by banks, with crises, which are not only not eliminated, but, on the contrary, acquire sharpness and universality precisely with the development of credit and credit money.

From this point of view credit as well as the so called 'credit creation' (Kredit schöpfung) of

[380]Marx 1981, pp. 648–9.

banks is wholly and fully connected and bounded to that system of production relations (capitalist), which generated this same creativity.

'Credit creation' can *never* be emancipated from 'golden fetters' precisely because credit money inseparably linked with real money. If credit money – whether in the form of banknotes, acceptances or giro-payment obligations – would be emancipated from gold, as the expansionists want, as well as credit utopians, of the type Proudhon, Gesell, – then with crisis inevitably would come the depreciation of credit money, and this 'would unsettle all existing relations'. That is why the legislation of all capitalist countries, contrary to the consecutive demands of Nominalists, so piously guards the gold reserves of central banks and establishes solid rules covering banknotes (but in the latest practice also checking accounts) with gold, and this curbs credit expansion. But thereby in crises 'the value of commodities is sacrificed (expansionists deny the necessity of this sacrifice. – *Z. A.*), to safeguard the fantastic and autonomous existence of this value in the form of money' (Marx). Thus, the link of credit money, and, consequently, also 'credit creation' of banks with money is expressed in the fact that the by banks created 'credit-money itself is only money to the extent that it absolutely takes the place (in circulation. – *Z.A.*) of actual money to the amount of its nominal value.' And as issuance is always possible above this limit, then the emitting authority must have in stock solid gold reserves, to pay with cash gold that excess mass of credit money. Therefore *the condition of gold reserves signals the direction of emission policy of banks*: after all, 'with the drain of gold its (credit money's. – *Z. A.*) convertibility into money becomes problematic',[381] and this threatens the fall of credit money, and consequently, also 'all existing relations', which neither government, nor central banks of capitalist countries can prevent.

That is why restraint of credit creation of banks by 'golden fetters' is not a tribute by legislation to metallic prejudices, but is *an objective necessity*. From these 'golden fetters' can *never* be freed capitalism. But recognition of the necessity of these fetters destroys all credit illusions, because at their basis lies the assumption of independence of credit money from real money.

* * *

When the classical (naturalist) theory of credit prevailed, then the answer to the question about limits of credit did not represent big trouble and therefore the problem was not sharpened. The answer read: bank assets are completely determined and limited by their existent liabilities, and with the latter are understood only accumulated deposits plus the

[381]Marx 1981, p. 648.

share and capital reserves of the banks. The bank cannot give more than it has. Moreover the bank cannot place in lending for the long term funds that it itself received on short term (until the claim).

This theory, as we have shown in our article 'The role of credit and the limits of credit expansion in capitalism',[382] was refuted not so much with logical criticism, as with the very facts. These latter clearly suggest that, firstly, the 'existent liabilities' do not at all limit lending, for this latter itself creates liabilities,[383] and, secondly, that short-term liabilities or kontokorrent [current account] liabilities of banks factually with certain boundaries are used for capital, *long-term* lending.

The first condition is the cornerstone of expansionist theory. However, refuting in their criticism the naturalists and proclaiming 'freedom of bank creation', the expansionists have gotten at close range before the problem of the limits of bank lending. The old limit rejected, a new limit must be found. It should be noted that in search of this new limit the expansionists do not at all show full unity: we have several solutions of this problem, with which we now familiarise.

2. Albert Hahn

As the most 'radical' leader of expansionist doctrine should be recognised, the same Hahn, who, to use Karl Diehl's expression, 'in the twentieth century stunned the world by an extravagant theory of credit'.

Hahn proclaims a *perpetuum mobile* of credit expansion and capitalist dynamics; as for such contradictions of capitalism, like *crises and unemployment*, then to eliminate them – is a mere trifle for 'correct monetary policy'. 'In a country with a single bank, – Hahn says, – or many banks with a coordinated credit policy, there cannot be a credit crisis ... as long as it is not desired and induced'.[384] Recognising the correctness of his theory, 'banks, – Hahn says, – would be able to dispose by appropriate arrangements of the harmful influence of depression (*Baisse*)'.[385] Hahn sees two possibilities for credit regulation of the conjuncture with the goal of eliminating crises. First, banks could stifle in the very beginning of the conjuncture growth (and consequently the crisis reaction to the upsurge) through very high interest rate. But this capability Hahn decisively rejects, because, of course, there is no reason to delay growth of

[382]Atlas 1928.
[383][For example by discounting bills of exchange.]
[384]Hahn 2015, p. 76. [We refer sometimes to the original (Hahn 1920). Some quotes translated by us.]
[385]Hahn 1920, p. 158.

production forces. He is more impressed by the second possibility of control, namely the *maintenance of eternally high conjuncture 'through ever-growing credit expansion*'.[386]
We do not have the possibility to dismantle here such utopian proposition of Hahn for resolution of crises, as lower interest rate, thanks to the possibility of credit expansion until zero (and even turning the interest rate into a 'negative magnitude!'),[387] or purchase *by the Exchequer* of surplus production to stockpile goods, which, by the way, has particular importance 'for political and military reasons'.[388] The fact that Hahn proposes his dubious instrument for imperialists, – this is curious enough and telling, but for us it is important now to establish only what Hahn considers possible and even necessary for 'ever-growing credit expansion'.
But in fact Hahn must be well aware that so called 'purchasing power', issued above the volume of *existent* commodity-circulation, hence, additional and redundant 'purchasing power', must act *inflationary*. This Hahn does not deny. But he calms down with the point, that if at the moment of credit expansion prices and demand exceed supply, then in the 'future' there occurs an equalisation,[389] and 'in general' (!) thanks to price competition there is a tendency to fall to the level of 'cost price'.[390] This tendency does not act in relation to agricultural commodities, but credit expansion is here not the cause: 'The reason lies in the law of diminishing fertility. By contrast, in relation to industrial commodities, when production develops, induced by credit expansion, connected with a transition to improved methods of production, "in the future" there inevitably will take place a reduction in prices even below the level preceding the credit expansion'.[391]
But these 'in general' and 'in the future' – are very hazy places in the conception of Hahn. Until the new commodities will be thrown into the market, created by lending of credit expansion to enterprises, many years will pass (Hahn himself says, that we are not talking about weeks, but about months, years and even decades), during which the country – sacrificed to the Hahnian illusion – will have a *disrupted monetary system* with all the charms of *inflation*. What this charm is and whether capitalist society reconciles with it during those *decades*, whilst to the market flows a new commodity stream, – this we leave to the judgement of the expansionists, to those of which, who have not yet lost sense of measure and reality, as well as understanding of elementary laws of circulation.

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[386]Hahn 1920, p. 159.
[387]Hahn 2015, p. 117.
[388]Ibid.
[389]Hahn 2015, p. 104. [Hahn 1920 p. 150]
[390]Hahn 2015, p. 104. [Hahn 1920, p. 151]
[391]Hahn 2015, p. 108. [Hahn 1920, p. 138]

So, credit expansion promises capitalism a 'golden age' of eternal and crisis-free upsurge. The only boundary, which, according to Hahn, can be encountered by credit expansion, – is *available labour force*. Credit expansion exhausts its capability only in the moment, when 'the last labour reserves of the country have already been used'.[392] This limit is nothing other than the *highest level of development of productive forces, as limit of every general rationalisation of social economy*. And the greatest 'miracle' is the point that for this there turns out to be no need of *any social revolution*, – it is enough to use the 'social recipe' of the modest bank director – Albert Hahn!

We have no need to lower down Hahn from these romantic heights to the sinful capitalist ground. This was successfully done by Hahn himself in his article 'Kredit' (1923).[393]

A *superhistorical* limit to credit – the productive forces 'in general' – Hahn puts forward also in this paper, however, brings with it an amendment, that undermines the very foundations of his conception. 'The limit (of credit expansion. – *Z.A.*), – Hahn says, – is achieved when even the most *strong changes* of distribution, – with detriment to net consumption, cannot involve new labour forces into the production of goods, – *a situation, towards which modern capitalist economy rarely proceeds, because conjuncture fluctuations, due to crisis phenomena, periodically bring with them strong delay of sales and limits production and disturbs the full use of all productive forces*'.[394]

To be sure from this phrase is fully clear the futility of that credit romanticism of Hahn, about which was spoken above. It turns out that credit 'in general', 'discussed purely theoretically', although also it can lead capitalism to highest development of productive forces (and consequently between production relations of capitalism and productive forces there is not any contradiction), but towards this the matter 'rarely proceeds' because crises... disturb the development of productive forces! Why then all his credit-romanticist reasoning? Obviously, it is necessary only for *apology of capitalism*, although Hahn's argument, aimed in this direction, is refuted by the observation of the same Hahn over several concrete phenomena of capitalism.

But with this little, we can easily prove, that the above adduced theoretical 'postulate' of Hahn about the independence of credit expansion from the patterns of [laws governing] circulation, on which properly also rests his whole romanticism, is refuted in this article by the same Hahn with a determination, deserving of praise.

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[392]Hahn 1920, p. 145.

[393]This article was included in a collection of journal articles of Hahn called *Geld und Kredit*, 1924 [pp. 39–59.]. We cite this article after the mentioned collection.

[394]Hahn 1924, pp. 55–6.

Hahn distinguishes *non-inflationary* and *inflationary* credit. The volume and capability for expansion of the former is contained by itself, namely is limited by the volume of savings (and this is entirely true). And 'as for the ability of banks above the frames of non-inflationary credit to provide inflationary credit, then generally it must be said that this ability is valid not only as an exception, as is usually considered, but as a rule, and in the *greatest volume*. The last decades, especially in Germany, represent by themselves nothing more than *one continuous period of almost uninterrupted provision of inflationary credit*'.[395] Thus Hahn wants to present the economic upsurge of Germany over the past decades (before the world war), as *consequence of credit inflation*.

However, all this is nothing more than a tribute to credit romanticism – one of the devices of apology for capitalism, – because several facts observed by Hahn himself refute this position. We noted that the credit-romanticism of Hahn rests on the assumption of independence of credit expansion from the patterns of circulation. Let us give the word to Hahn himself for a refutation of this central premise of his understanding. In section VI of the mentioned article under the title 'Credit and crises' Hahn says, that 'the conjuncture, created with credit expansion, may end or break with more or less crisis phenomena because of two reasons...'. The first reason consists in the following.

> In a state with pure-paper currency, where there is not addressed any attention to the relation of the value of domestic to foreign money, it is possible to permanently continue the increase of the mass of money. *Contrariwise, this is impossible, if in the concerned state gold currency is supported and if the state wants to maintain a determined parity of domestic to foreign money*, because the circulation of money, running parallel with the increase of the monetary mass, leads by itself to short or long-term outflow of gold or convulsion of the parity of domestic to foreign money, so that from inter-currency grounds the termination becomes necessary of the growth of the monetary mass. This happens, in this way, that the mass of provided credit is limited. This in its turn is achieved by means of raising the discount rate and with this increase the cost of credit.[396]

All this leads to 'the fall of industrial profit, wages, and more or less extensive unemployment'.[397]

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[395]Hahn 1924, p. 47.
[396]Hahn 1924, p. 57.
[397]Hahn 1924, p. 58.

Thus credit inflation is curbed by *golden fetters*, which either fetter such growth of credit expansion in the very beginning, or smothers the economic upsurge at its culminating point. Hahn does not bring proof, that capitalism can do without gold currency. But this he could also not prove. And once gold currency is necessary, this signifies the baselessness also of all the theoretical arguments of Hahn, related with the unrestricted and creative role of credit expansion. *But the recognition of the connection of credit expansion with gold currency is nothing but the refutation of the promoted postulate of Hahn about the independence of credit expansion from the patterns of circulation. On the contrary, precisely the latter wholly and fully limits credit expansion or so called inflationary credit.* And this connectedness of credit expansion with golden fetters was recognised, as we have shown, by Hahn–the practician, although also in full contradiction with Hahn–the theorist (a similar contradiction of theory and practice we will meet below in the analysis of the doctrine of Schumpeter).

Now turning to the second cause of crisis, as conclusion of credit expansion.

'But even if, – Hahn says, – a collapse of credit expansion does not follow from currency-policy grounds, then *nevertheless credit expansion of its own can lead to crises*. Credit expansion means, as noted, also rise of production. *But protracted production upsurge is impossible if there is no corresponding expansion of consumption*'. If this does not happen, then crisis is inevitable. The path of credit expansion – is the path of continuous and ever amplifying restriction of consumption. Meanwhile, against the conception of Tugan-Baranovsky, production for the sake of production is impossible. Hence it is clear that even if unlimited credit expansion were possible (that is, distracting from the patterns of money circulation), then the economic upsurge, induced by it, would include a contradiction in itself, *inasmuch as this expansion intensifies the contradiction of production and consumption and consequently accelerates the inevitable and independent–of–credit–expansion crisis*. And if so, it means also the development of credit expansion, carried out by Hahnian methods, has herewith its *self-limitation*, because the generated by it phenomenon *paralyses* this expansion. Such are the necessary conclusions from the by Hahn recognised second reason, generated by credit expansion.

Recognition of these 'two reasons' means, as we have shown, the utter bankruptcy of the credit romanticism of Hahn and is absolutely incompatible with the following thesis of Hahn:

'Eternal prolongation of credit conjuncture, *discussed purely theoretically* (!), can be achieved in such a way, that with lagging sales constantly again will arise demand, thanks to

credit making solvent [payment capacity]'.[398] Of the incompatibility of this 'purely theoretical' thesis with facts, evidently, also Hahn himself is aware, for in his final 'practical' summary about the tasks of credit policy he says the following:

> Credit expansion is one of the strongest means – perhaps in general the most powerful means – in order through uttermost use of production forces to accelerate economic development of the country and bring it to the highest prosperity. However the path of credit expansion goes through a relative expropriation of money owners, through worsening (depreciation) of the existent money in the national economy and through the danger of crises of sales, from which modern capitalist economy also without this suffers enough. One can therefore consider the tasks of target-conscious credit policy to be to conduct the economy through the Scylla of economic decline and the Charybdis of depreciation of money and crises.[399]

This, of course, already is not credit romanticism, but wholly 'reasonable discussion'. But this discourse means the complete bankruptcy of the theory of Hahn in the face of concrete facts.[400] The so called 'object of knowledge' of the theory of Hahn is entirely cut off from the 'object of experience'. Credit romanticism of Hahn breaks in smithereens on the golden barrier; credit romanticism is pincered by golden fetters, and from these fetters it can be released really only by a purely metaphysical theory.[401]

3. Werner Sombart

We now turn to the theory of credit and particularly to the doctrine about limits of credit of

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[398]Ibid.

[399]Hahn 1924, p. 59.

[400]Rudolf Stucken likewise notes that Hahn and Schumpeter in their latest publications already more significantly determine the limits of credit creation, – at least, for countries with gold currency, – than in their previous works. With this, from the point of view of Stucken, are eliminated some places vulnerable to critique (*Angriffspunkte*) from their doctrine (see Stucken 1929). This is said too softly: in fact these *Angriffspunkte* of their doctrine are places of the necessary and essential elements of their common theoretical conception. And if so, then we cannot speak about the correction of some mistaken places of their theory, but about the bankruptcy of the entire conception as a whole.

[401]In analogy with Hahn's social-credit illusions has come forward in German literature Gottfried Feder. 'In any case, – Feder says, – we believe that this form of financing (on the recipe of Hahn. – Z.A.) opens before us *unforeseen and grandiose possibilities in relation to use of the natural wealth of the country, improvement of the means of connection, and so on ... Every people is wealthy insofar as it can organise its labour* (our emphasis – Z.A.). According to Feder, capitalist society, regulated with the correct credit policy and generous credit emission, is able best of all to organise social labour and, consequently, lead to *most social wealth*! (Feder 1921).

Werner Sombart, who also paid tribute to the credit-romanticist illusions. *The eclectic Sombart* also in the theory of credit wholly maintains his usual style. On the one hand, he goes far *beyond* Hahn, considering, that also labour force is not a limit of credit expansion, and on the other hand, returns to the liability and naturalist theory, stating that '*deposits are in the most part short-term and ... not suitable* for lending in fixed capital' (for *Anlagekredit*).[402]

This as if amounts to the adoption of the basic thesis of the naturalists – contingency of assets on existent liabilities or the *prius* of liabilities, in contrast to the *prius* of assets in Hahn. But nothing of the sort: Sombart – is a hot expansionist, even hotter than Hahn himself!

It is far from useless to familiarise with this 'pitched' expansionist theory of Sombart, for here Sombart undoubtedly is original, he does not just copy Hahn.

From the classification of credit given by Sombart (classifying phenomena – in this is the talent of Sombart!) from the viewpoint concerning us, the most interesting and of principal significance is the distinction of forms of credit according to the third classification feature, – 'according to the origin of credit means'.[403] Here Sombart establishes that 'the means, by which credit appears, that is the means, through which persons, who do not have money, acquire purchasing power, are formed either from public revenue, or from circulating capital, *or out of nothing* (*aus dem Nichts*): The first two types of means can be united and counterposed to the third type'. This latter Sombart calls with a difficult to translate term *Anweisungskredit*, and the first two *Übertragungskredit* (roughly – 'transmittable credit'[404]). Under *Anweisungskredit* ('instructed', 'ordered', 'mandated' credit), which we will call 'creative credit' [*tvorcheskim kreditom*] (which corresponds to the content invested by Sombart in this term), Sombart understands what is commonly called 'credit creation' [*sozdanie kredita*] (*Kreditschöpfung*). But Sombart considers this concept as having multiple meanings, and therefore unclear.

About 'credit creation' one can speak in three different cases, namely when the granted credit is issued: 1) above the debtor's assets; 2) above the assets of the creditor and 3) *above society's assets*. With this, Sombart emphasises, 'only in the last case there is *Anweisungskredit*, purely creative credit'.[405]

Thus, credit can be extended not only above the funds, which are available to borrowers and

[402]Sombart 1927, p. 185.
[403]Sombart 1927, p. 176.
[404]Sombart 1927, p. 177.
[405]Sombart 1927, pp. 177–8.

lenders, but even above 'society's assets'. Under this last Sombart understands not *only means of production*, but also *labour force* in that volume in which it before lending existed in society. He stresses that with the by 'creative credit' provided production the purchasing power exceeds the labour force found in actual stock. This credit, hence, 'always represents itself a purchasing power, *which can be satisfied only by additional labour*' (Sombart's emphasis. – *Z.A.*), and 'from this follows that *Anweisungskredit* has very important meaning for the emergence of new capitals'.[406]

So, we see that Sombart in his radicalness left Hahn himself far behind, inasmuch as he believes that *through credit capitalism not only is able to liquidate unemployment, but even makes necessary the amplification of 'productive labour force'.* Thereby Sombart ostensibly removes also the by *Hahn* established limit and sees in credit a directly wonderful force, creating both new labour and new *capital.* Here it is already as if all limits for credit expansion were completely eliminated: it is impossible to imagine a more powerful lever of progress than credit!

But such conclusions from the theory of Sombart, although they also correspond with the precise given positions, would be too hasty. Here Sombart just like Hahn and Schumpeter, pays only a tribute to economic (credit) *romanticism*, but *realism*, stemming from genuine empiricism, – is yet to come...

Turning to the problem of 'limits of credit', having cardinal meaning for practical questions of economic policy of the bourgeoisie, Sombart leaves the clouds of romanticism and takes to the hard ground of reality.

'The limits of credit', he establishes in relation to: 1) credit in general, 2) 'transmittable credit', 3) 'creative credit'. Let us examine all these three cases.

1) Here we learn that 'for all types of credit the common limit is *the amount of stock of existent money* (*Bargeldvorrat*) of the country, consequently, in normal times the amount of *gold stock*, inasmuch as note issue is based on a well-defined quantitative proportion to gold reserves'. With this Sombart refers to Marx, who pointed out the inability of the credit system in capitalism to be emancipated from the metal limit. However let us note, that Marx pointed out, *why* this is impossible, and this impossibility, which becomes real in *crises*, Marx derived from the general contradictions of capitalism. Meanwhile Sombart simply lumps together on one heap the above–Hahnian illusions with Marx's theory, which, as heaven from earth, differs from these latter...

'Existent money' in modern conditions is needed in the following situations: a) for offsetting

[406]Sombart 1927, p. 178.

the balance of payments between countries, a) inter-bank offsetting, c) payments in small turnover, as, for example, in the tram, restaurant, theatres, and so on, d) for paying wages of workers, e) for payments of farmers, especially where these are small farmers (peasants).[407] All this, of course, is entirely correct, but at the same time, very little linked, as we will show below, with the romanticism of Hahn and of Sombart himself.

2) In respect to 'transmittable credit' the limit lies in the *existent volume of savings*, and this limit can never be broken (here Sombart only repeats Hahn).

3) As for 'creative credit', then such, firstly, has limits common for all types of credit, – the volume of existent money reserves; furthermore, 'creative credit' has also a special border consisting in 'the ability of capitalist economy to expand' (*Ausdehnungsfähigkeit der kapitalistischen Wirtschaft*). In turn, this 'ability' is defined: a) from the subjective side as 'service-capacity' (*Leistungsfähigkeit*) of capitalist manufacturers in the intellectual and moral sense; b) from the objective side of this 'ability' is created the possibility of growth of: 1) material capital, 2) labour force, 3) sales [realisation]; finally, c) 'ability to expand of the capitalist economy depends on smooth, uninterrupted work of the capitalist machine, that is on the correct flow of the economic process, especially on the precondition of constant proportionality of industries, so as not to have any convulsions'.[408]

True to his, as we said, 'classification method of study' Sombart here from a purely German [sic] meticulousness lists possible restrictions of credit expansion. But for all its fullness this classification of brakes of expansion still cannot be recognised as satisfactory, because among all these 'brakes' are not set any *internal and patterned [law-governed] connections* and not identified the conditioning and the conditioned factors.

In fact, can one really say that the limit of expansion of capitalist economy (and, consequently, credit expansion) is given by the capability of expansion of 'material capital' and labour forces? Such limit is really operative only in *organised social economy*, the direct purpose of which is the most rational organisation of 'things and people' for the greatest fulfilment of needs, in the given social collective of individuals. To the contrary, in a *capitalist economy* as the direct goal or motivating stimulus for development serves the *obtainment of profit* by capitalists or the possibility to create value and *surplus value*. If there is not this possibility, the capitalist does not obtain from the 'combination' of things and people any profit, then also the stimulus of development is paralysed, *even though social needs are fulfilled only in the most insignificant degree and even though there was the existence of a mass of free 'material capital' and labour forces*.

[407]Sombart 1927, p. 181.
[408]Sombart 1927, p. 182.

Further in Sombart, along with labour forces and 'material capital' as a limit is specified the capability of expansion of 'sales'. Pointed to as a special, *independent* of this latter factor, is the mentioned necessary 'constant proportionality of production' and 'smooth, uninterrupted work of the capitalist machine'. But it is quite clear that these are not two independent factors, but two moments – cause and effect. It is obvious that the capability of sales, if the Narodnik-Luxemburgist theory of the 'third person' is rejected, is conditioned by this same 'proportionality of production', which in fact under capitalism is not and *cannot exist*. From the disproportional development of capitalism (including here disproportion between branches of production, as well as disproportion between production and consumption) follows the *limited ability of sales* (crisis of sales, as expression of the industrial crisis) and from this latter the inability to *realise profit*. With the presence of these latter 'limits' of general economic expansion the other limits disappear: a) availability of labour force; b) 'material capital' and c) 'service-capacity of capitalist entrepreneur in the intellectual and moral sense'. As soon as there is disproportion, crisis and the lack of profit – *'material capital', labour force and 'service-capacity of capitalist entrepreneurs' cannot limit capitalist expansion, because exactly in these moments, the first, second and the third are found in huge excess*.

As we can see, Sombart simply mixed the limits of economic expansion in general and limits of *specific-capitalist development*, the particularity of which is precisely *that it because of its internal contradictions is not able to use all available in society capability of development, and at a determined stage of evolution is transformed into a brake of economic expansion in general*.

But can one say that the established by us general limits of capitalist expansion are at the same time also limits of credit expansion? Here we encounter the second mistake of Sombart – *the mixture of the general limits of capitalist expansion* (which therewith are incorrectly established by him) *with the limits of credit expansion*. This error is quite similar to the previous one. The by Sombart given solution of the problem of limits of credit expansion (*Anweisungskredit*) – is no more than a truism. 'Generally', of course, there is no doubt, that credit expansion can not give more than that which capitalist economy itself is able to give. *But like capitalist production has its own specific limits different from the general limits of economic development, so also credit-emission, that is 'credit creation', has its specific limits*.

In its turn this mistake of Hahn as well as of Sombart is based on the false treatment of the essence and function of so called 'creative credit'. The only thing, that *Anweisungskredit* can

'create' – are means of circulation, not capital and not even money, but only *token money*, wherewith

> credit money is itself only money in so far as it absolutely represents real money to the sum of its nominal value. ... Hence we get forcible measures, putting up the rate of interest, etc., in order to guarantee the conditions of convertibility to gold.[409]

That in the final light the expansionists themselves too, but in full contradiction with their own theory, but in agreement with reality, have to, though in covered form, recognise this limit, – that is not difficult to show for the analogous Sombartist theory, as well as for the theory of other expansionists – *Schumpeter, Prion, Hawtrey* and others.
In Sombart this recognition is hidden behind the by him established common for all types of credit, and therein included 'creative credit', limit, which consists in *the amount of stock of existent money*, and inasmuch as the monetary system is based on gold, then in the amount of *gold stock*.
But recognition of this limit deprives every meaning of all other imaginary limits set by Sombart for credit expansion. Concretely this means that if the banks ceteris paribus 'made' too much means of circulation, if their 'purchasing power' has become significantly in excess of the existent mass of *realised* commodity values (expressed in gold, consequently in the sum of commodity prices), then the reassessment of these tokens of value is inevitable. And as gold remains under the former 'assessment' (because its value is not affected by 'creative credit'), then all begin to demand from the issuer the conversion of 'tokens of values' into real value – gold. As a result the gold stock decreases, and credit expansion is replaced by credit restriction. Thus, this golden limit *is not independent and final, against Sombart's view, but serves only as exterior expression of the disturbed* proportionality of the capitalist system of production. That is why Marx speaks about the metal limit, as about an 'imaginative barrier of wealth', that exactly also is lost sight of in Sombart, who here is trying to build on Marx. If the mentioned proportionality would be constantly maintained (which, as we have shown elsewhere, is not and can not be in capitalism because disproportion is inherent to capitalism), then there would not be this 'imaginative barrier', because 'with the development of the credit system, capitalist production continually strives to overcome ... the metal barrier'.[410]
But, having recognised this 'imaginative barrier of wealth' in the quality of a limit of credit

[409]Marx 1981, pp. 648–9.
[410]Marx 1981, p. 708.

expansion, Sombart herewith put a cross also above all other falsely by him set limits, and at the same time a cross over expansionist theory itself. Because it turns out, that credit expansion is not at all related to general economic limits of economic development in general and directly, not at all to the limits of capitalist expansion, *but to one thing only, to the capability of such an expansion of the credit–monetary circulation, in which there were maintained a determined proportion between gold reserves and emitted means of circulation*.

Insofar as disproportionality, inherent to capitalism, is manifested also in all forms of bank credit without exception, to that extent there continuously takes place this reduction and expansion of gold stock, which is falsely interpreted by theorists, as an independent limit and regulator of credit expansion. *This is not a limit and not a regulator of credit expansion, but only the external form of manifestation of internal patterns and contradictions of credit expansion*.

But a recognition of this 'imaginative' barrier knocks out, as we have shown, from the Sombartist theory the ground for romanticism. The credit romanticism of Sombart is as firmly tied by golden fetters, as the romanticism of Hahn!

4. Schumpeter and Prion

The same failure befell also the credit romanticism of another expansionist – Schumpeter. This economist, on the one hand, recognises, that 'creative credit' or, as he puts it, 'lending to production through ad hoc created purchasing power' (which is also referred to by him as 'forced saving' – *gezwungenes Sparen*. – *Z. A*.) 'principally describes the method, which provides economic development in an unclosed national economy'.[411] In another work he puts it even more definitely, emphasising, that 'these methods of financing ('creative credit'. – *Z.A*.) should be considered as properly normal and even more, as the solely possible'.[412]

But, on the other hand, along with this 'theoretical analysis of existing things' and so on, Schumpeter encounters the same limit, on which the theory of Hahn and Sombart broke, – gold. Schumpeter recognises, that his theoretical 'position is too much at variance with reality in order to be able to recommend a set out train of thought as practical credit-policy guidelines',[413] and 'discussing reasonably', recommends the most thorough way to bind

[411]Schumpeter 1911, p. 214.
[412]Schumpeter 1927, p. 87.
[413]Schumpeter 1927, p. 98.

credit expansion is the 'golden brake' (*goldene Bremse*), that is do away with that which in theory was recognised, as 'properly normal, and even more, as the solely possible'!!![414] A brilliant destiny of the theory, in the recognition of the author himself, is completely overturned in practice!

But this contradiction of theory and practice is nothing other than the expression of the internal defectiveness of the theory itself. The difference between Sombart and Schumpeter is only that in the former the defectiveness of theory is expressed by inherent contradiction between elements of the theory itself, whereas in the latter the defectiveness is expressed in the contradiction between the theory (which is only in words free from contradictions) and practice (policy). Essentially invalid remain in equal degree both the theory of Sombart, as well as the theory of Schumpeter.

The same must be said also about Willi Prion [1879–1939]. This author in a whole number of his works, in particular in a number of articles, placed in *Handwörterbuch der Staatswissenschaften*,[415] develops purely naturalist, consonant with perspectives of classical theory on bank credit. However a whole number of positions, advanced by Prion in his [1926] work on *credit policy* (collection of articles), give us reason to believe that Prion adjoined towards expansionist theory.

Rejecting the main thesis of the naturalist conception, Prion proceeds from the entirely correct position, that 'banks can also provide credit without having for this to dispose of corresponding alien capital, or without having to use their own capital'.[416] We know, that in this case credit should be considered as *form of circulation* or realisation, that not any capital with this act of lending can be created, because the bank emits neither money nor capital, but means of circulation, which only *legitimise* the credit emission, created in the process of *commercial credit* [that is bills of exchange].[417]

But Prion adheres to a different point of view.

> They (the banks. – Z. A.) themselves create, – Prion says, – new means of payment, which they provide to their clients under the commitment of repayment from the side of the latter. Provision of credit is associated with the creation of money, or, as can be expressed differently, through credit is issued new money. When the bank issues the new money, then the creditor in any case receives money, for him there is no

[414]In detail we analysed Schumpeter's theory of credit in our article 'Role of credit...' (1928, no. 3).
[415]See Prion's articles 'Basic problems of banking policy' and 'The organisation and the foundation of operations of commercial banks'. [Prion 1924.]
[416]Prion 1926.
[417]See our article 'Toward a theory of bank credit' (1929).

> difference between new money and existent loan capital: *credit is for him loan capital, which serves as supplement to the earlier available to him existent capital*. But furthermore, this credit signifies an increase in money capital in general: loan capital, which features in the national economy, is increased by that sum of credit (emphasis ours. – Z. A.).[418]

Mixing means of circulation with money, money with capital, the credit function with capital-formation and capital-distribution with the function of capital-circulation (commodity realisation), Prion entirely naturally walks to the most important conclusion of expansionist theory, that *credit issuance is creation of capital*. He argues that by lending through issued funds the volume of capital is increased of the borrowers, and, finally, that such increase of the mass of capital is *fully regular* [*zakonomerno*: law-governed].

But with the adoption of this thesis it becomes entirely unclear why the banks *accumulate savings* and pay for them *interest*, as soon as they can create capital '*aus dem Nichts*'. If we accept this position, then one needs to throw aside as of no economic importance the savings and bank accumulation, to which Hahn dared to go, who therefore proved to be more consistent, then Schumpeter, because the latter does not deny the point that 'the energy, through which are saved up funds, is certainly the *essential element* of the fate of the nation and its future'.[419]

The same inconsistency is also in Sombart, who along with 'creative credit' speaks also about *übertragungskredite* ('transmittable credits'), – *although by the logic of things 'creative credit' completely excludes any necessity and expediency for the banks and for the national economy to employ 'transmittable credit'*.

Prion stops halfway and cannot resolve to go to the end after Hahn in the romantic heights. Similar to Schumpeter and Sombart, Prion first pays tribute to credit expansion, as the method of capital lending [*finansirovanija*]:

> Thus, – Prion says, – credit creation (*Kreditschöpfung*), which is associated with increased mass of money is not only bearable (*erträglich*) for the national economy, but may even be accompanied with favorable effects, because it stimulates the entrepreneurial spirit, increases production of commodities and contributes to a more proper distribution of revenues.[420]

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[418]Prion 1926, pp. 29–30.
[419]Schumpeter 1927, p. 85.
[420]Prion 1926, p. 32.

Yet further we again encounter also in Prion the contradiction common to the whole school of expansionists, which can also be called *the school of credit romanticists*. Indeed from all the reasoning of Prion it would follow, that there is need of every encouragement to this kind of credit expansion, which has not any specific capitalist limits and for which there are not written laws of monetary circulation. Prion should have to recognise that the limit of credit is not conditioned by specific-capitalist contradictions, that is that the limit of credit expansion is the volume of existent labour force (Hahn) or even more than that – the potential capability for expanding that productive energy, the labour force (Sombart).

But nothing of the like is claimed by Prion, who in contrast to Schumpeter wants to 'discuss reasonably' also in theory. From the given romanticist illusions Prion abruptly turns to *real capabilities* of using credit expansion. Asserting the necessity to finance production through *Kreditschöpfung*, Prion immediately warns for 'passion', speaking about the 'correct degree' of this lending. If *die Kreditschöpfung der richtige Mass überschreitet* ('if creation of credit exceeds the correct degree'), then *the beneficial effects of this wonderful 'creation' turn into its opposite and as a result a profound convulsion assails the whole national economy*.[421]

This is already completely not similar to Hahn and Schumpeter (in theory). Prion cannot *substantiate* that very 'degree', *which he nevertheless recognises*. The limit of credit expansion, for Prion, thus exists, but it is *unknowable*, as a sort of Kantian 'thing-in-itself'... Leaving unknowable the objective limit of credit expansion, Prion appeals to bank 'experience', which in contrast to Prionist theory *subjectively* constantly perceives this limit and is orientated to it. '*The solvency [payment capacity] of the bank*, – he says, – *determines the bank-technical (?) limit of creation of credit*. It is calculated by bank policy, resting on experience'.[422]

Needless to prove that this is not a solution of the problem, but a retreat of theory before the difficult task and is far from being 'in full battle order'. Economic theory must reveal the *objective cause* to subjective actions and reveal those *objective patterns*, which determine bank experience. It was necessary to show at what precise point the bank, through the creation of credit, is deprived of solvency and, consequently, forced to curtail its emissions. It was necessary, further, to show when and why credit expansion becomes needed and when credit restriction needed. Therefore the appeal to subjective bank experience we consider, as the whole bankruptcy of the Prionist version of expansionist theory. This version, certainly quite 'practical', likewise breaks on that same stone (existent[-money] – gold!), on which

[421]Ibid.
[422]Prion 1926, p. 34.

broke the versions of Schumpeter and Sombart.[423]

5. Hawtrey

As for Hawtrey, whom Hahn himself unequivocally counted to his school, then in him there is in general very little romanticism, and from the beginning dominates a fully realist-practical analysis of credit .

True, Hawtrey acknowledges that a bank can 'create credit' (which is not denied also by us) and that this stimulates the *development of production*. However Hawtrey relates quite soberly to this ability of expansion by 'credit creation' (Creation of Credit [in English in original]), putting credit expansion in quite narrow frames. That Hawtrey in contrast to Hahn is not a supporter of a *perpetuum mobile* of credit expansion, can be seen from the following of his arguments on this question.

'It is easy to see, – Hawtrey says, – how the line of least resistance will always lead to greater and greater inflation. If an inflation of credits once begins, the consequences will be felt in a withdrawal of gold'.[424] But, perhaps, the latter is not so bad, perhaps, regardless of this, one must continue the line of 'least resistance'?

Nothing of the sort. Hawtrey, adhering to completely sober views, equally sober, as also the views of Schumpeter – in practice or policy.

> If it tries to make up the shortage of currency (imaginary. – *Z. A.*) by further issues, and does not at the same time insist on a high rate of interest, the inflation of credit will quickly be intensified, the fresh supply of currency will be steadily drained away into circulation, and the withdrawal of gold for export will continue. There will soon

[423]In recent German literature appeared a new work of Honegger, whose author defends the conception of the expansionist school and gives an anti-critique to Adolf Weber, Edgar Jaffé, Heinrich Mannstaedt. In his positive part Honegger is more than weak and not convincing. The by him given solution of the central problem of the limit of credit in general boils down to the point that credit, based on national economic confidence, cannot cross this limit in trust. If in the national economy created credit instruments is above this limit, there arises 'credit uncertainty' (*Kreditunsicherheit*) that binds the capability of further 'credit creation' (Honegger 1929, p. 92) Such a 'solution' to this problem is very vague and hazy. Stucken (1929) in his review of Honegger's work indicated, that the disappearance of trust in credit means of payment is a consequence of restrictions of credit expansion as a result of inflation. However, also falling confidence in the 'credit instrument' and restriction of credit expansion are the consequence of deeper reasons, that are neither noted by Stucken nor by Honegger. But Stucken, of course, is quite right that the limits of credit expansion cannot be found in confidence, as a purely *psychological factor*, because this factor itself is objectively-economically conditioned. Moreover in Honegger is obtained a clear 'vicious circle'. Confidence falls as the result of excessive credit expansion, and expansion is excessive because the limit of trust is broken. In general expansion is excessive because it is excessive!

[424]Hawtrey 1923, p. 133.

> follow a renewed clamour for more currency, and, if the same situation is dealt with in the same way, it is inevitable that the system by which the note issue is related to the stock of gold will break. The moment the free payment of the legal tender notes in gold stops, they will begin to fall to a discount (i.e. there appears a premium on the metal. – *Z. A.*), and the foreign exchanges, already up to the export specie point, will become more adverse still. The failure to maintain specie payments marks the cutting adrift of the country's currency system from that of the gold-using world; it means, further, that business, which till then has been stimulated by the inflated turn-over of credit and therefore of purchasing power, begins to be disorganised by doubt as to the value of the monetary unit. Its value is palpably falling, but no one knows how rapidly it will fall: it cannot be permitted to fall indefinitely, or all measure of value will be lost, but no one knows when the limit will be reached or a recovery [restoration] will begin.[425]

So Hawtrey does not doubt in the necessity to restore convertibility into gold and the necessity of a credit restriction for paralysing extreme expansion. He, as we see, draws in gloomy colours the repercussions of credit inflation, as a result of excessive 'credit creation'. Hence the necessity for so called 'control over currency'. As means of this control serves the 'contraction of credit', to which is devoted a special chapter of his book *Currency and credit*.[426] Consequently contraction of credit is a means by which gold, having left in light of excessive credit expansion the country's borders, may be again settled in place. The contraction of credit can be achieved by direct limitation of lending, as well as by increasing

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[425]Hawtrey 1923, p. 134.

[426]The action of credit contraction (so called credit restriction), induced by previous excessive expansion of credit, Hawtrey depicts as follows: 'The contraction of the consumers' outlay is proportioned to the restraint on production, and the restraint on production is governed by the restriction of the merchant's purchases. If the home dealers alone are subject to the contraction of credit, the restraint on production is only partial; if home dealers and export dealers are both subject to it, the restraint is complete. *This gradual diminution of the consumers' outlay is of the essence of currency control. If the consumers' delay has become excessive this is due to a too profuse creation of credit.* In the first instance a credit expansion stimulates production; it is when production ceases to respond easily to the stimulus that prices begin to rise. Inflation consists in the spread of the infection of high prices through production to the consumers' income and thus to the consumers' outlay. When the whole productive machine is working at a high level of money values, and markets become unduly attractive to foreign trade commodities, imports increase, exports decrease, and a balance of indebtedness has to be paid. If matters are allowed to drift, the balance is paid in gold till the gold is exhausted. A *contraction of credit* , by impelling merchants to increase their sales and to diminish their purchases, helps to effect an immediate redress of the adverse balance of indebtedness and to preserve the stock of gold from further depletion. But a radical cure cannot be effected till the cause of the disorder has been removed, i.e., till the high level of money values has been reduced' (Hawtrey 1923, p. 121).
With this Hawtrey correctly notes that when analysing the impact of credit contraction on circulation and production one must take into account the country's relationship with foreign credit systems: 'Thus the attachment of a portion of the mercantile community to a foreign banking system weakens the effect of the contraction of credit upon production' (Hawtrey 1923, p. 115). 'A country, whose foreign trade is all or nearly all financed abroad, has less power of stimulating exports and repelling imports by means of a credit contraction' (Hawtrey 1923, p. 117).

the rate of interest.

However the attraction of gold from abroad is possible only in the case credit expansion did not yet decisively disorganise the system of monetary circulation: 'The two conditions, – says Hawtrey, – that must be fulfilled if a high rate of interest is to attract loans from abroad are that the solvency of the borrowers and the stability of the currency must command the confidence of the foreign lenders'.

Hawtrey firmly is holding on to the so called 'gold standard'. *Precisely thanks to the fact that the currencies of all 'civilised' countries are based on gold, credit expansion cannot unlimitedly and excessively expand*.[427]

The need of convertibility curbs credit expansion – that is the leitmotif of Hawtrey, wherewith, unlike Schumpeter, Hawtrey sees no need in a demarcation of 'laws of theory' and 'laws of life'.[428]

But, having included the gold standard in the theory of credit expansion, Hawtrey in the final light turns out to be as helpless in the cardinal question about the limits of credit expansion, as the above analysed Prion.

Hawtrey seeks refuge in cash [existent] money:

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[427]Hawtrey gives a thorough analysis of international fluctuations of gold and the role of credit in this process. Here are not installed the 'lending points', that is margins of discrepancy in interest rates of different countries in one and the same period of time. 'As a result of the general prevalence of the gold standard, rates of interest in different centres are linked together. They are free, however, to vary within limits, "lending points" as it were, not unlike the specie (gold – *Z. A.*) points of the foreign exchanges. If an extra 1 % on a three months' bill is just enough to attract a French lender to the English market, then the English bank rate cannot be more than 1 % above the French. Should the difference exceed this limit the remittances from Paris to London would speedily necessitate a rise in the French rate.' But this tendency operates only in case the gold standard is not broken; with the existence of that latter there may also take place counteracting factors (Hawtrey 1923, p. 122).

[428]Hawtrey considers convertibility of banknotes and deposits for gold an universal means against excessive credit expansion. Therefore he objects against artificial restrictions of credit expansion of deposit banks. He sides with bank liberalism and warmly defends the principle of *laisser faire*. 'One bank, – Hawtrey says, – cannot be more liberal than the rest in granting and discounting bills without having to meet an adverse balance at the Clearing-House. This operates as *an automatic check on the inflation of credit* . One bank may, it is true, adopt a lower standard of cash reserves than another, and may increase its profits at the expense of its power to maintain cash payments. But the narrower its margin of cash the less scope it has for inflating its loans. If its reserve is already cut down to the minimum sufficient for its day-to-day needs, the slightest laxity in the extension of loans will put it in difficulties and compel it to borrow' (Hawtrey 1923, p. 208). Thus Hawtrey believes that every banker, shall be interested stakeholder to maintain the necessary level of his reserves availability and accordingly restrain his credit expansion, and 'where he to reduce his reserve, he would only hamper his own freedom'. From this Hawtrey quite consistently comes to the denial of the expediency of legislative regulation of the reserves of deposit banks, adopted in the USA in connection with the establishment of the Federal Reserve system. He believes that with this system 'just at the time when banks ought to be using their reserves, they cannot pay them out without reducing them below the legal proportion'; moreover, 'the serious weakness in the system is that it does nothing to prevent that inflation of credit which leads to the depletion of the reserves' (Hawtrey 1923, p. 209). Of course, the Federal Reserve system can neither prevent general, nor credit crises, which can take place with compliant (before the moment of pressure) reserves. However also Hawtrey himself cannot offer anything for the prevention of not only general, but also specifically-credit crises, because his liberal principle in the domain of banking activities opens wide a scope for the deployment of capitalist disproportionalities.

> ...When, – Hawtrey says, – a general shortage of cash does occur, this is a *sign* that there has been an *undue expansion of credit*, and that is a matter for which responsibility rests not with the individual banker but with the central bank as the representative of the State. So long as the ordinary banker takes care that his assets are good, and does not swell his loans and discounts beyond the due proportion to his deposits, he is doing his duty to society.[429]

The space underlined by us in this summarised reasoning of Hawtrey in the quote has a very important meaning. The point is that Hawtrey does not at all consider cash, as a *limit* of extension of credit, but only as a *symptom* of already accomplished 'unhealthy' extension of credit, wherewith directly following this is emphasised that 'the ordinary banker takes care that his assets are good, and does not swell his loans and discounts beyond the due proportion to his deposits'. Consequently, this must be understood so, that a *general* restriction of cash [existent] money happens under the *conservation* of the 'due proportion' of assets and liabilities of individual banks. This is the most interesting point about the conception of Hawtrey. Why did the expansion of credit prove '*excessive*' if every single banker maintained 'due proportion' of assets and liabilities? The reference to cash [money] *disappears*, because one asks, why cash was suddenly insufficient, as long as 'due proportion' of assets and liabilities was maintained? Obviously, the former norm of cash became insufficient in light of a *general* excessive credit expansion. At the same time this excessiveness follows from a restriction of cash. Thus, the restriction of cash derives from excessive expansion of credit and excessive expansion of credit – from a restriction in cash. In the same exact vicious circle helplessly spins our Russian expansionist – Shaposhnikov.[430] It is obvious that between cash and the expansion of credit there is a *functional* connection, but not a *causal order*. If the bank increases cash, then it ceteris paribus restricts the relative volume of its lending; and if it expands the relative volume of lending, it herewith restricts cash. As for Hawtrey, he finds a way out of this vicious cycle in the same way that Prion found it – a reference to 'practice' or 'experience'. On the other hand Hawtrey drops the responsibility for 'excessive credit expansion' not on the bankers, *which actually implemented this expansion*, but on the 'central bank, as a representative of the State', which, he says, is insufficiently 'experienced' and skilful in 'controlling' circulation by means of its credit lever. The strain of cash is turned only in a *symptom* of excessive

[429]Hawtrey 1923, p. 207.
[430]Considering that the limits of credit expansion to be cash secured deposits and checking accounts, Shaposhnikov (1927, p. 27) herewith uses as sole evidence a reference to Hawtrey! But Hawtrey talks about restriction of cash as about a *symptom* of excessive credit expansion, which is not one and the same thing!

expansion, but not at all in the limit of it.

By this path the indicated contradiction is removed, but then credit expansion is devoid of any *real* foothold, and therefore *concrete limits* of this expansion cannot be specified. Obtained thus is a rather strange situation: there is no doubt that there is a certain determined limit of credit expansion, about which the fluctuation of cash constantly signalises, but in what this limit consists is a complete mystery! As for 'control over circulation', then with the inability to determine a concrete limit of credit expansion, it operates through credit restriction only *post factum*; with this path one can only *correct* the accomplished 'excessive' expansion of credit.

And so also Hawtrey does not solve the problem of the limit of credit expansion. But such a solution cannot be given on the basis of expansionist theory. We have seen that on this 'golden barrier' abut Schumpeter, and Sombart, and Prion, and Hawtrey, and to jump through this barrier without *abandoning the original point of their conception they were not able to*.

Insofar as Hawtrey, although also not sharing romanticist illusions, all the same accepts their thesis about *the patterns of the development of production exclusively on the basis of 'pure' credit expansion*, he too is unable to determine the limits of credit expansion, for it is impossible to establish, in what precise volume production can be expanded with the given method of lending. And that 'golden barrier' ('symptom'), on which Hawtrey abuts along with other expansionists, as we have seen, does not give the solution to the problem. On the contrary, recognition of this barrier cannot be regarded by us otherwise, than as the *factual rejection of the starting point* – the regularity [*zakonomernosti*] of expansion of production on the sole basis of credit expansion only.

6. Restoration of the 'gold standard' and 'credit creation'

After the general passion for nominalism during the war, when nominalism was a suitable theory to justify paper-money inflation, in bourgeois circles there came a sobering. The principle of the 'gold standard' received general, one can say, worldwide recognition. On the other hand, likewise by all the fact was recognised of indirect lending of the war *in the form of inflation of bank credit*.

Gustav Cassel, author of *Memoranda on the world's monetary problems*, pointed out that 'government finance is not the only factor to be taken account of in the process of inflation. *Every extension of bank credits beyond the limit set by the fresh savings put at the disposal*

of banks is apt to cause inflation'.[431] Inflation of bank credit – 'this is in fact what has been going on since the war in a good many countries', – says Cassel.

Inflation during the war in all its forms has already so much managed to suck out the juices of the world economy, that the point of view of Cassel has not met objections in business and government circles. In particular the inflationary impact of bank lending during the war was unanimously acknowledged at the Genoa conference and recorded in its conclusions.[432]

However the Genoa conference did not only proclaim the need to return to the 'gold standard'. The fact of active influence of bank lending on commodity prices during the war gave ground also for such conclusions, in which *credit romanticism* found its reflection – the idea of the general regulating and stabilising role of bank credit. In this respect it is characteristic that one will not meet any objections to the statements of chairman of the Finance Committee at the Genoa Conference, *Laming Worthington Evans*. 'In this sense the regulation of prices, – Evans said at the [second] plenum of the conference on 3 May 1922, – boils down to the regulation of credit. Experience, made since the war, by the Bank of England, as well as by the Federal Reserve departments in the United States, once again showed us, how sensitively prices react to changes of credit conditions ...'.

The Finance committee of the Genoa conference recommended a '*coordinated world credit policy*, thanks to which the big banks will get the capability to inform a *more stable character of the general level of prices*'. The 'directors' of the fate of capitalism in Genoa put forward a conception, which the 'socialist' Hilferding in 1912, in the pages of the social-democratic *Die Neue Zeit*, considered to be an absolute truth. And the same Worthington Evans saw in world credit policy a means to fight with European unemployment.[433]

It is known, that from the 'coordination of world credit policy' absolutely nothing came out, yes also could not come out, inasmuch as there exist profound economic, and consequently, also political contradictions between imperialist states.

After new inflation outbursts in Germany and France one finally managed to bring a stabilisation of the currency on the basis of the 'gold standard'. *But to stabilise currency – this does not mean to stabilise conjuncture*, and the hope of Evans to eliminate European unemployment and stabilise the conjuncture in no degree was materialised. Now, after the American stock market crash of late 1929, with the existence of the world crisis also for

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[431]Cassel 1921, p. 25.

[432]London memorandum (part 2: Restoration of Europe). http://discovery.nationalarchives.gov.uk/details/r/C4210066 [Genoa conference held in 1922.]

[433]Genoa minutes 1922. [No exact reference found in English] [In a 1944 article on the settlement reached at the United Nations' Monetary and Financial Conference at Bretton Woods, Atlas also reviewed the efforts of previous international financial conferences.]

Evans it must have become clear that his reference to the omnipotence of the Federal Reserve system is, to put it mildly, completely unfounded...

To the 'gold standard' returned all countries. For us here it is important to emphasise that the necessity to restore the 'gold standard', among other things, was motivated also by the fact that it is *necessary for curbing credit expansion*. This is precisely the practical conclusion, to which, as we have shown, have come, though in clear contradiction with their own conception, the leaders of the expansionist school. In the report of the English committee for the study of problems of currency and foreign exchanges, the so called *Cunliffe Committee* [1918] noted that, 'long experience has shown', the automatic mechanism of gold money circulation 'to be the *only effective* remedy for an adverse trade balance and an *undue growth of credit'*. This committee insisted that the source to cover the costs of capital investment for economic reconstruction of countries after the war *would not be new credit, but only genuine savings*. These costs 'cannot be met by the creation of fresh purchasing power in the form of bank advances to the government or to manufacturers under government guarantee or otherwise'.

So, the Cunliffe Committee did not soar in the clouds of credit romanticism and, fully aware of the vital interests of capitalism, demanded the same 'golden brake' for credit expansion of banks, the necessity of which, as we have shown, was recognised also by Schumpeter. This 'brake' is, of course, absolutely necessary for capitalism, because *without actual money – gold – there can be neither credit, nor capitalism in general. But this very 'gold standard' and 'control over circulation', which on the basis of the first must bring central emitting banks, to put a cross over the illusions of the credit romanticists, also in its turn, gives rise to new contradictions, which we cannot here consider*.

7. Goodliffe, Lampe and the 'ethics' of the naturalists

As we have shown, expansionists, starting with broad and attractive credit-romanticist illusions, encounter the contradictions which credit expansion brings with it. To eliminate these contradictions they, as practicians, recommended such measures, which bind credit expansion, thereby undermine credit romanticism.

Unlike the expansionists the largest part of the naturalists do not suffer the credit-romanticist disease. They are strict 'realists' and do not give to credit the significance of central regulator of economic dynamics. Credit – is 'just' a special way to transfer *things* from hand to hand – and nothing more. What kind of credit creation can be spoken of?

> You cannot, – says Walter Goodliffe, – create a credit: 'ex nihilo nihil fit', and apart from its basic commodity or service, credit – and money which is credit made visible – is nothing worth. There must be an exchangeable something from which a credit derives, and any medium representative of such credit can only be valuable while that something exists, and is available.[434]

In order to immediately dissociate from the illusions of credit of MacLeod, Goodliffe as a motto of the first chapter of his work chose a phrase from Shaw [1927]: '*You cannot create a credit'*. But this 'saying' carries a purely declarative character and has 'academic' significance in the worst sense of this word. The same declarative character carries the indictment by Goodliffe of 'instruments of bank credit' (credit money. – *Z. A.*) that they are, supposedly, 'bad', surrogate money. This is motivated by the point that the specified 'instruments' lack the attributes of 'sound money': 'they are not issued by constitutional authority, are not based on the national credit, nor does parliament exercise any control on their issue'.[435]
But a fact remains a fact: let Shaw say to the bankers 'you cannot create credit', these bankers create 'credit instruments' and are widely used by them for their active banking operations. To deny this fact is impossible, – it is known to any capitalist. But from the point of view of Goodliffe such type of operations of bankers can not furnish entrepreneurs capital – they render them only 'temporary support' under fully sound security.
In light of the necessity to keep one's assets in liquid form, 'no bank can loan its credit to customers with safety, unless the security pledged is not only sound but readily realisable in the open market; and no borrower can with safety employ bank credit for other than temporary purposes without incurring grave risk should the credit be withdrawn'.[436]
But is this the case in reality, is it true, that banks 'loan their credit' only for temporary purposes? The theory of Goodliffe, as also of all naturalists, is in conflict with reality, since practically there is no possibility to distinguish between 'financing' [*finansirovanie*] and 'lending' [*kreditovanie*]. *And if so, then there is no possibility to restrict the use of the by banks created 'credit instruments' only to 'temporary purposes', and not to long-term financing of industry*.
This is the reality, and the comical thing is that, acknowledging this latter, Goodliffe expresses 'regret' that this is the case. '*However, unfortunately (sic!), the demarcation of*

[434]Goodliffe 1927, p. 2.
[435]Goodliffe 1927, p. 30.
[436]Goodliffe 1927, p. 32.

the bounds between commerce and finance, under the existing system, is so complex and involved, that it is difficult to differentiate the use of bank credit for finance – which concerns only the employment of capital, and for commerce – the actual exchange of products, with which alone currency is concerned'.[437]

Ethics we set aside: let us grant Goodliffe regret apropos this – science before this has no concern. The latter cannot but be interested in the following. *If the by Goodliffe marked differentiation of bank credit in reality is completely unfeasible, if the banks emit means of circulation, finance from these funds industry, then how is it possible to deny credit expansion in the sense of Hahn–Schumpeter–Hawtrey*? Of what consists after this the declaration, with which Goodlife began? And further, if the naturalist acknowledges the fact of financing of industry through issuance of means of circulation by banks (on which also rests the whole conception of expansionists), then where is the limit of 'credit creation' or credit expansion? To what boundaries can the banks expand this 'creative credit' shamefacedly recognised by some of the latest naturalists?

On this question in recent German literature tries to give an exhaustive answer a naturalist of, we would put it, 'latest formation' (that is acknowledging the noted fact) – *Lampe*. This author made an extensive criticism (albeit rather confusingly) of the *Economic theory of bank credit* of Albert Hahn. Of course, this criticism should have included in itself a positive answer to the question of boundaries of credit expansion, which could be opposed to the solution of this problem by the expansionists.

Lampe favourably differs from other naturalists, in that he directly speaks about 'credit creation' by banks, as about a *fact*. This saves him from those frills to which commonly resort the naturalists. Lampe points to the volume of reserves of the social product and to the 'economic possibility to deliver for restoration of the social product an equivalent of the taken (product. – *Z.A.*)'.[438] In these limits credit expansion does not lead to inflation, and the latter Lampe believes, in opposition to the expansionists, is *harmful*, inasmuch as it *disturbs the equilibrium of the national economy*.

Further Lampe notes, that in case of financing of industry through ad hoc created purchasing power, either consumer demand must be decreased (or, as he expresses it, – 'there must be an abstraction of demand from the social product') in the amount, taken by the receivers of credit; or these products must be replaced by others. Both of these possibilities Lampe denies. 'On the one hand, the demand for life-necessity products is highly inelastic; on the other hand, the capability of reproduction of these products in a given production period is

[437]Goodliffe 1927, p. 34.
[438]Lampe, 1926.

insignificant. Consequently, with these two facts are set very narrow limits of credit creation'.[439]

Credit expansion (in the sense of Hahn–Schumpeter) can be based, mainly, on the reserves of the social product: 'when the stock due to additional demand of the receivers of credit, will be threatened by exhaustion, and manufacturers present high demand for means of production, then from the supply side will act a trend of raising prices',[440] wherewith this trend will carry a purely inflationary character and therefore would have from the point of view of Lampe a negative meaning.

Lampe comes to conclusions in which there is quite a lot of 'common sense' and which are a completely natural reaction against the theoretical liberties of the expansionists. In his summary Lampe says:

> Even under the significance taken in the abstract of a research premise – the 'law of slow turnover',[441] and 'plan-commensurate economic leadership' – a 'golden age of economy' cannot be achieved by unlimited credit creation. Any illusions, connected with credit creation, collapse completely, if it is considered, that credit creation exactly disturbs the 'harmonious combination of the social product', prompting the disturbance of the equilibrium of the movement of labour forces, while the 'law of slow turnover', counteracted in each of the given cases, by the inflationary tendencies of credit creation, is completely indeterminate.[442]

Here, indeed, are found the desired words. Lampe, along with Diehl,[443] quite rightly recognises the illusion of a 'golden age' of capitalism, created after Macleodist recipes. And it is likewise true that this 'harmonious combination of the social product' (that is proportionality of social production) in certain conditions can be disturbed by inflationary tendencies, caused by 'credit creation'.

But can these trends be eliminated? Is it possible to confine credit expansion within the frame of limits, the defined by Lampe 'reserves of the social product', and so on? Naturalists and Lampe along with them answer positively to this question. And it is necessary to observe that the views of Lampe in this question do not rise above the vulgar notions even of the same

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[439]Lampe 1926, p. 129.
[440]Lampe 1926, p. 128.
[441]'Law of slow turnover' – so we translate the formulation *Trägheitsgesetz des Verkehrs* of Zwiedineck. This 'law' consists of the point that in economic turnover there is inherently a certain resistance to oscillations of prices (*Preisbewegung*) provoked by one or other factors (see Zwiedineck 1909, p. 84).
[442]Lampe 1926, p. 129.
[443]Diehl 1927, pp. 582–95.

Goodliffe. The whole matter allegedly lies in the bad mode of activity of bankers and in the dangerous theoreticians, who justify this mode of activity. Instead of objective analysis of social factors, *stemming from the very nature of the capitalist mode of production and causing the given 'abnormal' (!) mode of activities of bankers, Lampe raises the normative question*: 'this' in capitalism can not and *should not be!*

Here is his last word: 'credits through savings (*Spar-Kredite*), if at all also can be replenished the additionally, productively applied purchasing power, then in any case only in an insignificant volume and always with a threat to the flow of economic life'.[444]

Such a normative ethical approach to the problem of credit expansion and its limits is received by modern German naturalists from their predecessors. Still *Knies*, who gave a critique of MacLeod, came to the same conclusions. Proceeding from a concept of credit, as transfer of things and so on, Knies set for credit a 'material border', – the limit of the expansion of credit, from his point of view, is *real capital* in its natural form of means of production;[445] so above the sum of national accumulation – savings banks neither can, *nor should* provide credit to their clients.

In later literature, for example, in Spiethoff or Beckerath, the same motive is repeated: *to create credit* and with it expand production is not allowed, because banks should not through their issuance finance industry, if they do not want to bear responsibility for the severe consequences of a 'foolish' policy of credit inflation.

Spiethoff came to the conclusion that the credit market [that is banks] may supply 'formal purchasing power (acceptances, notes, papers [*Buchgutschriften*]) only *temporarily*, and always with *undoubted dangers to the national economy*'.[446]

Likewise also Beckerath in his study of *Money markets and capital markets*, noting the inadmissibility of the use of funds of the money market for the needs of the capital market, points to the dangers that are involved in this kind of policy,[447] as though on the latter the patterns [*zakonomernosti*] of capitalist dynamics actually depend. But how little Lampe adds to Beckerath, and this second – to Spiethoff, – and, finally, the last – to the old Knies!

As an immutable tradition of vulgar economy, it looks at the surface of the monetary–credit sphere of contradictions of capitalism and, by virtue of its limited bourgeois horizon, does not see their real roots.

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[444]Lampe 1926, p. 130.
[445]Knies 1879, p. 213.
[446]Spiethoff 1909, pp. 30–1. [Paraphrased.]
[447]Beckerath 1916, p. 110.

The normative approach to the problem of credit expansion is proper likewise to American theorists and practicians of the naturalist direction. Take, for example, a fairly typical address by William Amasa Scott in *Investment Bankers' Association of America*. Scott categorically claimed, that 'when commercial banks create their own demand obligations, either in the form of checking accounts or notes against investment securities, they are creating an obligation that they may not be able to meet'. This he explains with the point that the funds, which bankers use in these cases, are inadequate for the purpose, namely: 'however productive the enterprises may be, which these securities represent, they only after a series of years, bring into existence an amount of production sufficient to offset the initial investment'.

So, the use of 'credit creation', that is to create termless debt obligations, with investment goals is not allowed; the exclusive purpose of these funds, as Scott notes further, – is meeting operating commercial needs, for example, to discount commercial paper, which in the shortest term is paid by debtors.

However Scott, like also the other Americans, has to admit that the reality is not such, as it is wanted by him. Bankers exactly are widely involved with investments through the creation of their own obligations.

> The result of such loans, – Scott says, – is overexpansion or inflation of credit, i.e. the banks have created obligations against themselves which they are not able to meet in the normal course of business. So long as business is prosperous all goes well; but as soon as there is a break somewhere in the industrial system and borrowers for investement uses are unable to pay, serious trouble follows (panic) ... Forced liquidation is a necessary outcome of overexpansion of credit caused by the exchange of investment securities for checking accounts, and if such forced liquidation is general throughout a country and attempted on a large scale, then ... commercial crisis is inevitable.[448]

A similar view was expressed by Geiger in the pamphlet *Financial readjustments* (1915). He also sees in the practice of lending through creation of 'obligations on demand' the cause of 'many sleepless nights for bankers'.[449] But is it possible to eliminate this 'insomnia' of bankers, is it possible to prevent crises? Carman[450] sees all evil in the point of the prevalent in

[448]Reprinted as 'Results of investments loaning by commercial banks' in Moulton 1917, p. 459.
[449]Reprinted as 'The misuse of commercial bank funds' in Moulton 1917, p. 451.
[450]Reprinted as 'The advantage of the draft over the promissory note in commerical banking'in Moulton 1917, p. 451.

America practice of credit obligations, the so called 'promissory notes', represent themselves 'a combination of commercial and investment credit'. And since obligations on demand should not, if they want to sleep peacefully, be used by bankers, – then Carman sees salvation in the rejection of promissory notes and 'book credit' (the creation of chequing accounts. – *Z. A.*) and a transition to the European method of lending *for drafts*.[451]

But in Carman certainly is an outdated picture about 'European *lending practices'. Also in Germany and in England the weight of draft lending is falling, and increasingly the dominant form of lending becomes chequing accounts. On the other hand, the transformation of capitalist banks from 'commercial' to 'investment' banks, which happened recently in America and [which was] named by Louis Brandeis a 'revolutionary change' in banking matters,*[452] *in equal degree is innate also to European capitalism*. After the publication of the study of Adolf Weber (1902) and of Wieser (1919), one can no longer talk not only about 'European' in general, but not even of 'English' lending practices, in contrast to the American, that is mixed 'investment–commercial methods'.

That is why the 'key of salvation' of Carman, proposed in his time for American bankers, is very, very rusty, and therefore unusable. For this fact, the so called 'Combined work', that is the universalism of credit methods of capitalist banks, we tried to provide a theoretical basis.[453] From our point of view, the propositions by the above mentioned American authors to restrict credit expansion with the goal of healing the 'insomnia' of bankers, that is prevention of crises (as though the cause of crises is in credit expansion!) by a framework of purely 'commercial credit' and refusal of financing ('investment credit'), are *absolutely unfeasible*. Such a restriction contradicts the specific patterns of the money market and bank credit and in general testifies to the vulgar, purely superficial perception and explanation of the contradictions, which volens nolens are observed by bourgeois practicians and theorists. *Naturalists observe the contradictions of capitalism, manifested in bank credit and believe them to be results from incorrect modus operandi (incorrect methods of lending) of bankers. From this their simple and naive recipes of healing the diseases of capitalism, their normative approach to the problem of limits of credit expansion. They do not understand a simple thing, namely, that these contradictions are inherent to capitalism, and that therefore, regardless of the 'modus operandi' of bankers, credit, as one of the immanent forms of the capitalist mode of production cannot but include these contradictions in itself. Precisely these objective contradictions of capitalism condition the*

[451]In Moulton, pp. 451–2.
[452]Brandeis 1914, pp. 26–7.
[453]See our article 'Money market and the contradictions of bank credit' 1929/30.

subjective actions of bankers, which the naturalist 'condemn' with as much vigor as naivety, not realising that another 'mode of action' of bankers is at all impossible!

What is the substantive difference between expansionist and naturalists in the given question? Both one and the other cannot, of course, not detect the *real* contradictions of bank credit. But both one and the other deny the *necessity* of these contradictions.

However they *deny these contradictions in different ways*. Marx found that '*banking and credit become ... the most powerful means of driving capitalist production beyond its own barriers and one of the most effective vehicles for crises and swindling*'.[454] The abnormality of credit from the point of view of both directions consists of the point that from time to time there take place 'crises and swindle', whose presence is impossible to deny. The naturalists believe that crises occur due to improper credit policy of *bankers*, which should not bring the capitalist mode of production beyond its own limits. The expansionists, conversely, see the abnormality of the situation in the point that limits are artificially placed to credit expansion; they seek salvation (only in theory) in unrestricted credit expansion to 'drive capitalist production beyond its own limits' and with this finish with the contradictions of this mode of production. They want to *eliminate* the contradictions of credit of one or another credit policy.

But neither restrictive, nor expansionist policy are in a state to eliminate the contradictions of credit and the credit system. These contradictions exist and will exist for as long as the capitalist mode of production, generator of these contradictions, is preserved.

The correct answer to the question about the limits of credit can be given only on the basis of Marx's doctrine about the cyclical motion of capitalism and the dialectical connection in this process of the basis of productive capital and the superstructure of loan capital. As a positive treatment of this problem is beyond the scope of our essay, we confine ourselves to the most general characteristics of this position, proceeding from which we have criticised bourgeois theorists.

The general limits of credit emission are entirely explicitly specified by Marx.[455] But the limits of credit emission should not be confused with the limits of credit in general,[456] with limits of *credit expansion*, which we understand not at all in the Hahnian sense (that is as credit inflation); such expansion signifies *expansion of credit in general, regardless of its sources and its funds, for example, accumulated or emitted*. What are the limits of credit

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[454]Marx 1981, p. 742.

[455]See previous quote (Marx 1981, p. 742) – *Z. A.*

[456]We consider it necessary to note that in our earlier articles on the subject of credit in the journal *PZM*, and in *Vestnik* the problem of limits of credit was considered largely one-sidedly, as a problem of limits of credit emission, and in consequence of this was incorrect.

expansion understood *like this*?

These limits are given by the concrete capabilities of the expansion of productive capital in the given segment of a cycle. It is obvious, that these limits reach a maximum, with an upsurge, a minimum – with crisis and depression. In the epoch of industrial capitalism 'the maximum of credit is the same thing as the fullest employment of industrial capital, i.e. the utmost taxing of its reproductive power irrespective of the limits of consumption'.[457]

If in consequence of the basic contradiction between the social character of capitalist production and private appropriation, at a known point of the upsurge with necessity comes crisis, then this signifies *the exhaustion in the given cycle all the possibilities of the expansion of productive capital and, consequently, likewise the possibilities of expansion of credit. Hence – sharp squeeze of credit*. With stagnation in business, that is depression, the limits of credit remain narrowed to the minimum, and in that moment it turns out to be impossible to use for lending *not only emitted, but also accumulated funds*. Here we have abundance of loan capital, which finds no application, because both production and circulation are squeezed and, consequently, also the limits of credit are squeezed.

If there is a depression or crisis, then so called *Kreditschöpfung* cannot help, because the pattern of the movement of loan capital in the final light is conditioned by the pattern of the movement of industrial capital, and not vice versa.

Insofar as there is an upsurge, which never and not in any case the banks themselves by their '*creation aus dem Nichts*' can create, there is an expansion of the limits of credit, and banks use all of their capabilities, *accumulation, as well as emission, in the bounds, permitted by the patterns of money circulation* (that is with preservation of free convertibility of credit money into gold, for which it is necessary to maintain a determined proportion of gold reserves to the emitted credit to ensure this convertibility), *for expansion of productive capital*, for the 'fullest employment of industrial capital ... irrespective of the limits of consumption'.[458]

But here we have not the mechanical expansion of credit as direct reflection of expanding industrial capital (naturalist theory), and not the reverse – the expansion of industrial capital because of the expansion of credit (expansionist theory), *but both one and the other*, that is the dialectical process of *interacting basis and superstructure*. This dialectical process is clearly formulated by Marx: '*A reciprocal effect takes place here. The development of the production process expands credit, while credit in turn leads to an*

[457]Marx 1981, p. 613. These words of Marx were said in an analysis of commercial credit, but they are valid in the determination of the limit of credit in general on a given segment of the cycle.
[458]Marx 1981, p. 613.

expansion of industrial and commercial operations'.[459]

Superstructure (loan capital, the credit system) is conditioned by the basis, but only *in the final analysis*, which means that, contrary to the mechanistic naturalist theory of the classics *credit affects production*, though contrary to expansionist theory, *credit is conditioned by the patterns of capitalist production and cannot go beyond the frame of the latter's intrinsic contradictions*.

Credit accelerates and enhances the upsurge, but at the same time aggravates and exacerbates the crisis. And contrary to the two basic bourgeois theories of credit and conjuncture, credit cannot but play this double role in the cyclic motion of capitalism. Contrary to the naturalists, credit and 'credit creation' cannot but force the upsurge (naturalists 'condemn' precisely such conduct of banks), but, contrary to the expansionists (who praise this 'creation') expansion of credit, credit 'creation', facilitating expansion of production, cannot call forth a *perpetuum mobile* of this upsurge, because it *only develops the inherent contradictions of capitalism and with necessity leads to crisis*, consequently, *to sharp narrowing of the limits of credit expansion, which in upsurge were widely extended*. From this is clear that *bankers are governed by credit and its limits*. These limits are the patterns of the cyclical movement of capitalism and that contradictory movement of real and loan capital which is exhaustively described by Marx: *banks can only better or worse adapt to these patterns*, but against all bourgeois credit romanticists, they cannot overcome these patterns. Bank policy and bank legislation of course affects the cyclical movement of production, but they do not affect it as to cancel the immanent patterns of this movement. That is why, for example, 'ignorant and confused bank laws, such as those of 1844–45, may intensify the monetary crisis. *But no bank legislation can abolish crises themselves*'.[460] Thus the limits of credit, against the naturalists, are not conditioned only to accumulation, against the expansionists – credit expansion is not unlimited, but strictly bound by the fundamental patterns of the cyclical movement of capitalism, including in this the patterns of production, and of circulation, and distribution, and consumption, as moments of a unity – the process of reproduction.

Thus there are no metaphysical limits of credit expansion, abstracted from the fundamental contradictions of the capitalist system and the general pattern of its movement. This limit of credit always is concrete, namely: it is conditioned by the concrete incapability of the movement of industrial capital in the given segment of a cycle. As expansion of production in capitalism with necessity is replaced by its compression, so also

[459]Marx 1981, p. 612.
[460]Marx 1981, p. 621.

expansion of credit is replaced with its sharp restriction, wherewith, of course, in the final light the motion of the superstructure is conditioned by the basis: meanwhile 'the superficiality of Political Economy shows itself in the fact that it views the expansion and contraction of credit as the cause of the periodic alternations in the industrial cycle, whereas it is a mere symptom of them'.[461]

From this it is clear that one or another way to influence the symptoms of the disease, does not mean to cure the disease: 'No kind of bank legislation can eliminate a crisis' (Marx), and consequently also unemployment and impoverishment of the working class, etc. The disease of capitalism is not given to cure by expansionists or by naturalists, for this is necessary the intervention of a surgeon, who would uproot the real reasons of the social disease, which led to the *general crisis* existing outside the USSR system of production, to the decay of capitalism, of its material basis and all of its superstructure. The decay of capitalism means at the same time the decay and degeneration of bourgeois economy. In this we could be convinced also by the example of the 'scientific', so to say, 'creations' of modern credit romanticist–expansionists.

[461]Marx 1976, p. 786

Chapter Twenty-One

'The Quantity Theory of Money (Essay of Methodological Criticism)' (1928)

Stepan Legezo

1. Introduction

Every theory is a reflection and a by means of a determined method conversion in the human head of reality. 'To see in theory the depicting approximate copy of objective reality, this is what constitutes materialism', says Lenin apropos this.[462] Hence: the scientific character of a particular theory is determined by its ability to give a relatively correct picture of objective reality, a relatively exact copy of it.

The theory, 'depicting' social-production processes and relations of exchange economy, is political economy.[463] Money is a socio-economic category.[464] Therefore the theory of money is part of political economy; only within its bounds and on its basis the theory of money gets its scientific significance.

However political economy deals not with exchange society 'in general', that is not with commodity production in its immediate concreteness, but with the economic categories of this society. And since 'economic categories are only the theoretical expressions, the abstractions of the social relations of production',[465] then, consequently, *the theoretical 'depiction' of the reality of exchange economy takes place in the form of abstractions of the social-production relations*. Economic categories: commodity, value, money, surplus value, capital, credit, rent, and so on – represent by themselves, thus, the theoretical expression of the abstraction of determined relations of production, or as Marx says elsewhere: 'forms of being, determinations of existence – and sometimes only individual aspects – of this particular [that is modern bourgeois] society'.[466]

Speaking, consequently, about the quantity theory of money, it is necessary to put the decisive methodological question, whether it depicts those real processes and relations of the socio-economic reality of exchange society, which hide behind the phenomena of

[462]Lenin 1908, p. 265. ['The recognition of theory as a copy, as an approximate copy of objective reality, is materialism'.]

[463]Against the claims of some Marxists that political economy studies 'only' capitalist relations of production, we believe that the latter studies the relations of production of exchange economy, taken as a whole, as combination of the historical moments: barter, simple commodity circulation, and commodity–capitalist circulation. Therefore in the following in all cases we will use instead of the concept 'capitalism' the concept of 'exchange economy'.

[464]Against the claim of chartalists who consider money to be a legal category.

[465]Marx 1963, p. 109.

[466]Marx 1986a, p. 43.

commodity–monetary circulation, or more precisely: whether it reveals the essence of these phenomena and, herewith, whether it establishes the real economic laws, governing the above listed processes and relations. It seems to us that only with such a statement of the question the task of methodological criticism of the quantity theory of money can be properly solved.

2. The essence of the quantity theory of money

What is the core, essentially defining, constitutive in the system of the quantity theory of money? If we leave aside all particular–specific features of this theory and take the most common–generic of its features, then this 'core' can be reduced to the following four positions:

First of all, with the quantity theorists 'commodity circulation (in the given case the capitalist process of exchange of things. – *S.L.*) is looked at exclusively in the form C—M—C, and this in its turn solely as the dynamic unity of sale and purchase'.[467] *Differently stated, capitalist economy (M–C–M) is reduced to a simple commodity economy (C–M–C), and the latter – to its natural form*. In fact, unity of sale–purchase is the characteristic form of exchange for the epoch of barter, for the epoch of natural exchange, where there is not yet commodity, nor money in the proper sense of the word. The unity of sale–purchase: this is the characteristic form of the exchange process for the epoch of the pre-bourgeois mode of production, – in which still only the process of formation of this mode of production occurs within the bounds of the natural form of production, but, herewith, also the process of the formation of the universal category of the exchange economy, the category of commodity. This is the epoch of the development of the commodity and the birth of money. Simple, expanded and universal form of value – are only aspects of the genesis of the commodity, – moments, marking themselves determined stages of the genesis of exchange economy. Here 'already' exists exchange, but not 'yet' circulation, because there is no money. All relations of exchange as of yet proceed in natural form. The universal equivalent, that basic monetary form of value, too is still naturalised, it is not sufficiently separated from the use property of the product. Only the fusion of the universal equivalent form of value with a determined thing turns it into money, and this real thing (commodity) into the material carrier of this form – into coin. In

[467]Marx 1987, p. 391. True, what Marx says here, relates to the quantity-theorist-classics, but these views on commodity circulation are characteristic not only for quantity-theorist-classics, but in general for all quantity-theorists. [For the sake of brevity from now on referred to as 'quantis'.]

this 'coalescence', by the way, consists the whole meaning of the leap from direct trade to commodity circulation.

By limiting commodity circulation to the formula C–M–C and understanding the latter, as unity of sale–purchase, the quantis thereby reduce the complexity of the capitalist process of exchange of things, proceeding in the form of commodity–(capitalist–)circulation, to simple, direct (natural) exchange of products. Hence we can derive the first position of the quantity theory of money:

Commodity circulation is natural direct exchange of products. Therefore laws of circulation of developed forms of exchange economy are reduced to laws of simple direct (natural) exchange economy.

This reduction of commodity circulation to natural exchange inevitably naturalises also the category of money. Therefore money in exchange for quantis proceeds in its natural form, in the form of a simple 'good', in the form of an ordinary 'property right', the distinctive feature of which consists only of the fact that it is 'taken by all in exchange for other commodities' (Fisher). The quantis represent to themselves the matter in such a way that commodity circulation is a process of exchange of things which can be accomplished in principle without money, but which gets technical facilitation with the introduction of one or other medium of exchange. So, for example, Hume believed that 'Money is only the instrument which men have agreed upon to facilitate the exchange of one commodity for another'.[468] Or: 'Money is nothing but the representation of labour and commodities, and only as a method of rating or estimating them'.[469] Roughly in the same spirit also Fisher defines money: 'Money never bears interest except in the sense of creating convenience in the process of exchange. This convenience is the special service of money'. In another place Fisher characterises the category of money as: 'Any property right which is generally acceptable in exchange may be called "money". Its printed evidence is also called money'.[470] J.S. Mill said the following on money: 'It is a machine for doing quickly and commodiously, what would be done, though less quickly and commodiously, without it'.[471] *Thus, starting from their understanding of commodity circulation, as unity of sale–purchase, the quantis define this naturalised category – money – as technical means of facilitating exchange, as an instrument of exchange.* Marx from of all this drew the following conclusion: 'If commodity circulation is looked at exclusively in the form C—M—C, and this in its turn solely as the dynamic unity of

[468]Hume 1889, p. 309.
[469]Hume 1889, p. 312.
[470]Fisher 1911, pp. 5 and following.
[471]Mill 1909, p. 488.

sale and purchase, the specific aspect of money as means of circulation is upheld against its specific aspect as money'.[472] According with the above we formulate the second position of the quantity theory:

Money is a technical means of facilitating direct exchange, that is money is an instrument of exchange.

But money in the quality of instrument of exchange is isolated in its function, as coin. And as the 'tendency of the process of circulation is to transform the coin from its metallic existence as gold into the semblance of gold (i.e. wear), or to transform the coin into a symbol of its official metallic content',[473] then on the basis of the economic law, which reads, that 'means of circulation, isolated in its function serving as coin, becomes a value token'[474] – money in the quantis is inevitably reduced to a token [or sign] of value and because of this takes on the laws of circulation of these tokens.[475] In this way, we can deduce the third position of the quantity theory:

Money is a token of value. The laws of circulation of value-tokens are the laws of circulation of money in general.

However 'in accordance with the law relating to the circulation of value-tokens ... prices of commodities depend on the volume of money in circulation, and not that the volume of money in circulation depends on the prices of commodities'.[476] Hence the fourth position of the quantity theory of money:

Prices of commodities depend on the amount of money circulating, because they are constructed in the direct exchange on the market, by simply contrasting two not on each other dependent magnitudes: money tokens and the commodity mass (two streams).

The value of money, in light of this, from the viewpoint of quantis, is nothing more than a nominal magnitude and measure, which manifests itself 'really' in the actual exchange, in the so called 'purchasing power' of money tokens.[477]

To proper theory of money relate only the last three positions. The first position is only a

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[472]Marx 1987, p. 391.
[473]Marx 1976, p. 222.
[474]Marx 1987, p. 391.
[475]Here a reservation is necessary of the following character. It would be correct to say that 'quantis reduce money to tokens [or signs] of values', only in relation to the classics (Ricardo-Mill), who recognise the substantial value of commodities and money. As for Hume and Fisher, who deny the substantial value of money, then in relation to them it would be correct to say that money is not reduced to tokens of value, but to tokens of price. However, in essence, both the tokens of value of Ricardo-Mill and the tokens of price of Hume-Fisher, – are one and the same, because for both the value of money in the end is deduced from a mechanical juxtaposition of two not on each other dependent magnitudes, – the commodity mass and money tokens.
[476]Marx 1987, p. 391.
[477]In this relation the quantity theory of money is close to nominalism. Not for nothing the early quantis Hume and Montesquieu were at the same time nominalists, while the modern nominalists Bendixen and Elster largely sympathise with quantis.

methodological premise of this theory.

From the above scheme of the main positions of the quantity theory of money it is clearly seen that the whole primitive edifice of this theory is built on very shaky foundations. In fact the assertion that the essence of money consists just of being an instrument of exchange, means that the essence is replaced with the phenomenon, it means to assert that the phenomenon coincides with the essence. But this at the same time means, to entirely abandon theoretical economy, because, as Marx points out, if the form of appearance coincided with the essence of things, there would be no place for science. In the quantis the form of manifestation – money, as instrument of circulation – coincides with the essence. In this respect the quantity theory of money is based on the theoretical foundations of vulgar economy. The vulgar understanding of the nature of money is predetermined by the wrong methodological assumptions, which, strictly, also give the content of this theory. Therefore: 1) identification of the methodological premises of the quantity theory of money *is the first objective of criticism*; 2) disclosure of errors in understanding of the quantis of the nature of money *represents the second task of criticism*, finally, 3) scientific substantiation of the concept of 'purchasing power of money' on the basis of the law of value and disclosure of the errors of the quantity theory of money in this area – *represents the third objective of criticism.*

3. Methodological premises of the quantity theory of money

Inasmuch as the position of the dialectical theory of knowledge is true, that method is the spirit of every cognition and that method is correlative with the object of this cognition, we can by logical means, through disclosure of the reverse connections of the main positions of the quantity theory, determine the object–methodological guideline, with the help of which this theory is constructed.

The determination of 'purchasing power' of money in the quantis follows from the reduction of the value of money to a coefficient of the exchange of money tokens over the mass of commodities.

The reduction of the value of money to a coefficient of exchange (and herewith also to value-tokens) follows: in some (Hume-Fisher) from the rejection, in others (Ricardo-Mill) from the incomprehension of the substantial aspect of the category of money.

In its turn the reduction of the value of money to a coefficient of exchange, and therefore also

to tokens of value, is only a consequence of the fact that the main characteristic of the essence of money is reduced to its definition, as instrument of direct exchange.

But an instrument of simple, direct exchange money can only be in such an exchange economy, where there exists the unity C–M–C, that is under the condition of reducing developed commodity circulation to a simple naturalised process, that is to the process where M acts in a still undeveloped natural-equivalent form.

And this latter follows from the understanding of commodity economy: first, as an eternal and principally-immutable system of production, and secondly, as a system, which organically is not connected by any internal unity, as a system, in which the subject of production is the individual household (Robinsonades of the classics).

All this taken together is, in turn, a product of apologetics of bourgeois thought. Ricardo, for example, believed, that society is nothing than a fictitious body, a mechanical sum of the individuals who compose it.[478] This viewpoint on bourgeoisie society, as a subjectless and mechanical unity, to one or other degree prevails in bourgeois *economic science* also to the present day.[479] Similar kind of views on bourgeois society as a trans-historical and undifferentiated category, closely connected with a metaphysical worldview, are typical of any theoretical thought of bourgeois ideologues and theorists. 'The individual and isolated hunter and fisherman, who serves Adam Smith and Ricardo as a starting point, is one of the unimaginative fantasies of the 18th century', Marx wrote in his time.[480] However, we know that the eighteenth century was the century of the heyday of the metaphysical worldview... Separate individual households, these Robinsonades, with which the Austrians 'start' and 'end', belong to the chimeras of the second half of the nineteenth century. In this sense the Austrians are the successors of the metaphysical guidelines on exchange economy, guidelines, from which Smith and Ricardo proceeded. But with the Austrians the consanguinity is found in mathematics, and the contemporary quantist Fisher with his formula 'Equation of exchange' illustrates the principles with mathematical theory, applied to monetary circulation.

Thus we see that both historically and logically the quantity theory money with its roots

[478]Rubin 1979, p. 236. [The phrase is Bentham's.]

[479]Struve, for example, also believes that 'the social connection in economy is an imaginary connection, and social economy is a pseudo-economy' (cited after Bazarov 1927, p. 164). Bazarov says on this subject, that 'for the bourgeois scientist the national-economic whole, is not a reality, but an abstraction and moreover an "epistemological abstraction"' (ibid.).

The same idea Sombart expresses, when he questions the presence of a unity of the world economy: 'individual national economies, – he says, – are becoming ever more complete microcosms, and the internal market increasingly overshadows the world market in importance for all lines of trade. At present, the individual national economies are drawn weaker into the world market, than a hundred years ago' (Sombart, *Die deutsche Volkswirtschaft im neunzehnten Jahrhundert*, cited after Luxemburg 2013).

[480]Marx 1986a, p. 17.

starts and rests on the metaphysical method of cognition. Capitalism, as an eternal and once and for all established category, and moreover as an epistemological abstraction, as pseudo-economy and so on, this is a metaphysical category. *But the metaphysical guideline on the subject inherently by itself already determines the fate of the quantity theory*. With such a guideline, completely is eliminated the basic premise of scientific cognition, the premise which consists in the fact that, firstly, 'the condition for the knowledge of all processes of the world in their "self-movement", in their spontaneous development, in their real life, is the knowledge of them as a unity of opposites', and secondly, that 'the splitting of a single whole and the cognition of its contradictory parts' is a condition of all cognition.[481] Without this methodological condition there is no scientific knowledge. Yet, from the viewpoint of bourgeois theory, capitalism, as a national-economic whole, is without internal, inherent in it opposites and possesses no contradictions. These opposites and contradictions, consequently, also are absent in economic categories: commodity, value, money, capital, and so on, which, in the quality of abstraction of determined social-production processes and relations, would have to be carriers of the contradictions, inherent in commodity economy. Yes and in general can that have a unity of opposites which by itself is not a living whole, a moving unity? Of course not. That is why quantis nowhere speak of contradictions in the above sense. That is why in them the movement of commodities is not a contradictory process, but their mechanical transfer from one hand to another. That is why in them money serves only as ancillary means of this movement. But just in this is the root of the methodological error of the quantis. This basic error determines all the rest.

4. The problem of the nature of money in the quantity theory

The inability to understand the essence of the phenomena of economic reality is an organic defect of bourgeois political economy. This is explained by its negative relation to the dialectical methodology of cognition. Hence, as a rule, in the theories of money of bourgeois economists there almost always there is lacking an analysis of the genesis of money, and in those in which it has a place, such as, for example, in the nominalists, the latter is turned into a purely formal, declarative postulate. Herewith in bourgeois economists remains covered and not understood the nature of money, thanks to which all theory of money usually becomes a purely logical and rationalistic system (Knapp). In other words, *the incorrect*

[481]Lenin 1976, pp. 358, 357.

determination of the essence of money leads to a wrong construction of monetary theory. Therefore *to give the theoretically correct determination of the essence of money is the starting moment* in the construction of the Marxist theory of money as well as in the criticism of bourgeois monetary systems.

As we have seen above, in the quantis the nature of money is reduced: in terms of form – to means of exchange (second position), in terms of content – to tokens of value (third position). Under what provision would these positions be correct? Obviously, under the provision of the correctness of the first position,[482] that is if circulation of commodities in developed exchange economy was reduced to direct trade, and if in such an exchange process money could step forth not as the immanent movement of commodities by way of their circulation, not as the 'converted form of movement of commodities', but as the outside-extraneous way of 'creating facilities for the process of exchange' (Fisher) as the 'way of facilitating the exchange of one commodity for another' (Hume). Then indeed money would be an 'instrument of circulation' in the sense, as the quantis understand it. The best money, undoubtedly, would be the cheapest and best adapted to this technical function money tokens. And then, indeed, the relation of commodities to the value of the money material, and therefore also to its amount, would be passive-indifferent, because, as Ricardo claims, 'the smaller quantity of money would perform the functions of a circulating medium, as well as the larger'.[483] The value of the money (purchasing ability) in this case would be reduced to a coefficient of an exchange of money tokens for commodity mass. And then, of course, one could talk of the correct 'depiction' of factual reality by the quantity theory, talk about its scientific-informative worth.

But the fact of the matter is that the question about commodity circulation in developed economy stands entirely different than this is represented by the quantis. Direct exchange was indeed once the determined form of the exchange process, and then it determined the essential characteristics of exchange economy, existing in formation. However *now direct exchange is a historically outlived moment*.[484] *It was replaced* (successively one after the other) *by a new universal form of exchange: initially simple commodity circulation, and then commodity–capitalist circulation*. Between these forms of exchange (direct trade and commodity circulation) there is a fundamental difference. 'The circulation of commodities differs, – says Marx, – from the direct exchange of products not only in form,[485] but in its

[482]And this latter would be true under the provision of the correctness of the methodological premises of the quantity theory, the premises, that we above refuted.
[483]Ricardo 1810, p. 2.
[484]See on this in Luxemburg 2013 [1925, pp. 273–80].
[485]Mill represents the matter otherwise. He believes, that the simple introduction of a particular type of

essence'.[486] In what does this difference consist? The difference is that *under direct exchange, we have a direct connection of exchange of one use value to another, under commodity circulation, on the contrary, we observe the splitting of this connection.* In the first case, each individual use value is opposed directly to another use value in its natural form, whereas in the second case, each individual use value is opposed to many other use values in their value form through the common to them all and in this sense universal form of value – through money.[487]

The point is that historically developing spontaneous exchange of things (C–C), on the one hand, 'breaks through all local and personal bounds inseparable from direct barter and splits the to each other conjoined moments of this exchange'[488] and on the other – 'develops the circulation of the products of social labour'.[489] Objectively the split of the moments of sale–purchase is reflected in the fact that in developed commodity exchange commodity-producers one time sell on the market a commodity, but at a different time buy many other commodities. Here 'a sale leads to many purchases of various articles' (Marx), to purchases, that are usually carried out in another place at another time. The split in space and the split in time of the moments of exchange therefore requires a kind of general form of connection – a constantly operating universal equivalent of exchange. From the general world of commodity values, in the end, is exuded this equivalent. To it also are equated in their movement the products of labour, henceforth they may not be exchanged directly.

But here it must be emphasised that the universal equivalent is separated from the world of commodities and is fused with a certain thing, adopting the form of money, in the same historical sequence, in which the conjoined to each other moments of exchange lose direct connection, that is the emergence of the category of money takes place in the extent to which

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exchange (monetary. - S. L.), consisting of the fact, that at first a thing is exchanged for money, and then money is exchanged for some other thing, produces no significant changes in the nature of the transaction... 'Things which by barter would exchange for one another, will, if sold for money, sell for an equal amount of it, and so will exchange for one another still, though the process of exchanging them will consist of two operations instead of only one... The relations of commodities to one another remain unaltered by money' (Mill 1909, p. 488).

[486]Marx 1976, p. 207.

[487]Wherewith the general form of value here necessarily is fused with some thing. *Until there is not this fusion, substantially, there is no money yet, therefore also no commodity circulation.* Even in cases where formally in history there already was an intermediary counterposing products to one another, but when this intermediary was an ordinary object of consumption (whether that object was jewelry, cattle or even gold) not standing apart in coin, not separated yet from its use properties, then the exchange factually carried the character of direct trade. *Here commodities though they measured their value in one or another equivalent, factually still were exchanged directly.*

[488]Marx 1987. [A paraphrase maybe of this passage: 'The division of exchange into purchase and sale not only destroys locally evolved primitive, traditionally pious and sentimentally absurd obstacles standing in the way of social metabolism, but it also represents the general fragmentation of the associated factors of this process and their constant confrontation ...' (Marx 1987, p. 332).]

[489]Marx 1976, p. 207.

from natural economy finally stand out private producers of commodities, dealing exclusively with the manufacture of products for exchange, that is in the same extent in which is created a society of free commodity-producers – commodity society. And this, in its turn, means, that on the market begin to function clots of indifferent human labour.[490] In other words, *labour that creates products for exchange, takes on a universal character, the character of human labour in general, that is the character of abstract labour*. The universality of labour, creating products for exchange, is, thus, the expressed alteration of the mode of production, the changing socio-economic structure of human society. Initially irregular and, to a large extent, accidental exchange of surplus products within the bounds of the natural form of economy becomes then a universal phenomenon, it becomes the social form of exchange of things, and social-production relations of people take the form of exchange relations. Exchange of things begins to take place in the form of the movement of values, rather than the movement of products. Hence the universal equivalent, as expression of universal labour, creating products for exchange, is itself the reification of abstract universal labour. Herewith, if by itself *abstract labour in general exists in all economic formations, then the form of exchange of things it becomes only in exchange economy with advanced commodity circulation*.

We for now leave aside the question of the contradictory character of the origin of money. Here is important to note only the fact that commodity circulation brings with it in exchange such a new quality, which in direct exchange still was absent. *And with this new quality appears the universality, as specific social form of labour, creating products for exchange, the universality, which materialises in money*.[491] Thus, the universality of labour acts in the quality of an abstraction of the universality of commodity production, in the quality of the abstraction of the bourgeois mode of production, which has become universal.[492]

In direct exchange there not is yet the element of universal labour, because there are not yet

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[490]'The general value-form, in which all the products of labour are presented as mere congealed quantities of undifferentiated human labour, shows by its very structure that it is the social expression of the world of commodities. *In this way it is made plain that within this world the general human character of labour forms its specific social character*' (Marx 1976, p. 160; author's italics. – S. L.).

[491]'*The separation and independence of the acts of purchase and sale is a general feature of the labour which creates exchange value*, whereas in barter the exchange of one discrete use value is directly tied to the exchange of another discrete use value' (Marx 1987, p. 328; italics of the author. – S. L.).

[492]It is understood that when we talk about the universality of commodity production, it must be grasped in a relative sense. It should be grasped so that here the matter is about such a degree of universality, which was sufficient, as an objective presupposition for the birth of money. It must be born in mind that commodity production itself grows on the basis of the destruction of natural economy, which a long time exists along and together with commodity production, wherewith only the capitalist mode of production gives commodity economy a character of universality. 'Capitalist production first makes the production of commodities general and then, by degrees, transforms all commodity production into capitalist commodity production' (Marx 1978, p. 34.).

universal exchange relations of production. There is, therefore, not yet the commodity, as such. There is, therefore, also not yet value, as determined form of exchange relations of production. 'The direct exchange of products has the form of the simple expression of value in one respect, but not as yet in another'.[493]

There is, consequently, not yet money as complete economic category of commodity society. *Only in the commodity circulation value takes the complete form of exchange relations of production – the form of money*.

It is hardly necessary to dwell on this issue in greater detail. The principal difference of direct exchange from commodity circulation is obvious. This difference is observed in the analysis of the development of the category of commodity, or more precisely: in the analysis of the development of the form of value. Precisely based on the analysis of the form of value, Marx determined the essential difference of direct exchange from commodity circulation and thereby revealed the nature of the commodity itself, as well as the nature of money. The quantis *do not see this difference, and they do not see it because they do not understand the form of value*. Incomprehension of the form of value follows from the point *that they start from an essentially invariant exchange economy*.

So, the first position of the quantity theory of money: *commodity circulation is simple direct exchange of products* – is not true, because it *finds its confirmation neither in the analysis of the history of exchange economy, nor in the analysis of daily practice of commodity circulation, in other words, it does not reflect reality. And therefore it is not scientific.* From this follows logically the falsity also of the second position: *money is an instrument of simple direct exchange of products*, that is an incorrect definition of the nature of money. Not being confined, however, with this formal conclusion, we examine the question about the false determination of the nature of money of the quantis in substance. To do this we will have to, at least briefly, outline the Marxist conception of the nature of money and to oppose to it the conception of the quantis.

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In what consists the nature of money in terms of Marxist theoretical economy? Insofar as money is an economic category and insofar as: 'economic categories are only the theoretical expressions, the abstractions of the social relations of production', *the nature of money has to be sought in the socio-economic content of the social-production relations of exchange economy*.

Let us examine this question.

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[493]Marx 1976, p. 181.

First of all it should be emphasised that commodity production – is a historically transient form of economy that emerges, develops and disappears. In terms of the Marxist method it is not an epistemological abstraction, but an essentially-determined whole, a living moving unity. It is first of all a unity of oppositions, that moves through the development of internal contradictions.[494]

In the quality of abstractions of determined relations of production the above named oppositions and contradictions are possessed also by economic categories. Hence to uncover the oppositions of economic categories – means to determine the oppositions of those socio-economic processes or relations, which express themselves in the given categories, that is to determine the real character of this relation, the actual content of it, and together with this also to uncover the nature of that economic category. *Therefore to reveal the basic opposition of one or other category and thereby to arrive at the fundamental laws of exchange economy constitutes the main task of scientific analysis.* Precisely so Marx proceeded in his analysis of the commodity.

Marxist theoretical economy for exchange economy establishes the following basic opposition. In pre-capitalist commodity economy: a) on the one side, – the social process of production, taken as a whole, that is the social character of the aggregate labour of society, and b) on the other side, the private character of separate labour expenditure. In commodity–capitalist economy there is the same opposition, but in a modified form: here private labour expenditure is collectivised, though the appropriation of products continues to remain private. But in one and the other case *private and social moments oppose each other, as oppositions of the whole*. In the category of commodity these oppositions emerge in the quality of the opposition between use value and value, between concrete and abstract labour, and, finally, between commodities, as embodiment of at once individual private and social labour, and money, as embodiment of universal social labour. In other words, the basic opposition of exchange economy, taken as a whole, is: private and social source, that is private and social labour.

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[494]The methodological presuppositions of Marxist theoretical economy boil down in the following positions.
Emerging initially in the quality of a special moment of the previous (natural) forms of economy, exchange economy then develops into an independent whole, which has its own special form and content, its special nature.
In its movement exchange economy goes through a series of stages, a series of qualitatively different, but in their basic nature identical moments (unity of identity and difference). Hence, barter, simple commodity circulation and commodity–capitalist circulation are only special moments of exchange economy, taken as a whole.
The movement of the whole, just as the movement of its moments, occurs through accentuation of differences in the bounds of undeveloped concreteness, through the transition of developed differences in opposition and of developed oppositions in contradiction. This entire process is a saltatory process.
Every developed whole possesses developed oppositions.

The interaction and struggle of these oppositions deploys the general evolution of exchange economy.[495] It is, so to say, the general line of movement.[496] Beginning in a distant epoch of pre-bourgeois mode of production, – in the epoch of the formation of commodity economy, – in the shape of insignificant differences these oppositions in the epoch of imperialism reach their highest development and turn into insoluble contradictions of the system of exchange economy.

But the process of the development of oppositions of the system by itself – is a contradictory process, a process of movement through leaps. The rise and resolution, the resolution and rise of new contradictions in the movement of the main opposition acts, therefore, like an objective law of development of exchange economy. The essence of this law boils down to the fact that the opposition between private and social labour on determined stages of the quantitative growth of the elements of exchange economy steps forth in such a contradiction, which make impossible the further existence of this economy without creating new forms of movement of oppositions. The creation of new forms of movement of oppositions marks itself the appearance of a new quality, in this case new relations of production.

In other words, it is a nodal point of the development of the commodity. *With these nodal points appears a new form of movement of the commodity, corresponding to the appearance of determined economic categories*. So, the developed opposition between private and social labour during the period of natural economy has led to the contradiction between use and exchange value, between concrete and abstract labour (in other words, – to the contradiction between the individual producer of commodities on the market and between unorganised bourgeois society, as a whole). The contradiction is resolved with the appearance of the category of money. In money the product, destined for exchange, received a special form of its movement – the form of commodity circulation, and human relations took the form of exchange relations. Developing in this new form of movement of commodities, the basic opposition of commodity economy is the contradiction between

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[495]Private and public, this is in general the main opposition, conditioning itself the evolution of human society during the entire history of its existence. The epoch of natural economy (primitive communism, the tribal system and feudalism), this is the long epoch of a continuous (initially slowly, but then more accelerating) process of the allocation private moments, that is the epoch of the disintegration of collective forms of economy and the formation of scattered individual households. And the farther and deeper this process went about, the more and clearly was observed the contradiction of the social and private moments. The great historical process has ended, finally, with the formation of exchange economy. *The contradictions of collective natural economy were solved with the formation of separate individual economies. However, this separateness immanently generated its opposition – bourgeois society, with its irresistible tendency to socialisation*. The same opposition – private and social - continues to exist also here, but manifested in a new form and on a new basis. The line of movement went in the reverse direction: from private to social. The contradiction of exchange economy will get its final resolution only in communism.

[496]"Those contradictions, which move and develop the whole system of social relations and its separate links, do not arise in every social category, taken in isolation, but within the system, taken as a whole' (Kon 1925).

social production and private appropriation. This contradiction, in its turn, is resolved with the emergence of the category of capital. In the category of capital the commodity once again received a special form of its movement. At the same time as simple commodity economy has become capitalist, the exchange relations of independent commodity producers took the form of capitalist relations. In its turn, the movement of capital after the historical line has created a new contradiction, the contradiction between production and consumption, a contradiction that on the basis of capitalism can no longer be resolved by the advent of new forms of movement of the commodity, that is the emergence of new categories. This contradiction is eventuated permanently and is once resolved in crises again on the same basis, which created it, that is on the basis of the contradiction between social production and private appropriation.

It is understood that the question about oppositions of exchange economy here interests us not in itself, but only in so far as it helps us to figure out why and in what ways economic categories emerge from the contradictory movement of these oppositions. In this case we are interested in the category of money. *The category of money, therefore, is the result of the contradiction between private and social labour.*

But as the resolution of the contradictions within the given quality is, essentially, not an elimination of these contradictions, but only an interposed form of the movement of oppositions, then M is, on the one side, – one of the forms of the historical movement of C and – on the other – the universal form of the logical movement of C, that is the form of commodity circulation as such. In the first case money appears as a way of ensuring the further movement of exchange society. In the second case money appears in every given act of the movement of commodities as a way of their circulation. In other words, in the first case we have the development of the commodity and the birth of the category money, that is the genesis of money, in the second case – the execution of the daily movement of commodities, that is the function of money.

But the logical is the completed historical. The logical in its movement reproduces all the historical moments.[497] *The process of circulation with as its 'foundation' money, has as its presupposition therefore the process of the genesis of money.* Only in the genesis of money is revealed its nature.

Hence, in order to understand how money circulates, we must first understand why it

[497]Man in the mother's womb repeats the entire traversed path of the historical development of the animal world. To understand the place which man occupies with other animals, it is necessary to approach him genetically. Likewise it is necessary to approach also the genesis of money, in order to understand its place in the series of other commodities.

circulates. Anyone who does not understand the question, why money circulates, does not understand also the question, – how it circulates, he, consequently, also does not understand the nature of money. In such a situation the quantis proved to be. Not grasped the question of why the money circulates, they do not understand either the question of how money circulates. By the way, also the mistakes of Marxists, who on some issues of monetary circulation roll to the quantis (Hilferding and others), follow from an insufficiently methodologically mature understanding of the nature of money.

To the question about why the money circulates, we have already partly replied in the analysis of the concepts of 'direct exchange' and 'commodity-circulation'. There it was noted that M is an instrument of connection of the split moments of exchange purchase–sale, and that this M, as unity and means of consolidating the unity of the moments of exchange, is the expression of the universal nature of labour, creating products for exchange. But there it was not shown why private and social labour stood between each other in contradiction and how this contradiction was resolved with the emergence of money. This is on the one hand. On the other hand, there it was not shown how the continuous process occurs of the contradictory movement of private and social labour – the process that manifests itself externally in the circulation of commodities.

First of all, on the contradiction, permitting the appearance of money. This contradiction consisted in the fact *that the product of private labour, acting in the market in the quality of a commodity, can be exchanged only as part of the aggregate social labour, that is as a part of undifferentiated labour in general*. The product, intended for exchange, had to possess two counter-posing moments: a private and a social: As product, produced by an isolated individual, it represented itself the result of private labour. As product, produced in a society with an unorganised division of labour and intended for the general consumption through exchange, it had to represent itself the result of social labour.

As long as exchange represented itself the unity of sale–purchase and carried a purely-limited, local character, these two moments coexisting in one product, do not enter between each other in resolute conflict.

Until then products can be exchanged among themselves not through contradictory movement (change of forms C), but by simple, mechanical opposition. But inasmuch as there is a gap between the acts of purchase and sale and inasmuch as the simple exchange of products is converted in 'the circulation of the products of social labour', then between these moments brew a contradiction. Private and social labour, in the end, entered between themselves in hard conflict. Further exchange already could not occur in the form of a simple

opposition of concrete products, products of private labour. Developed exchange required the separation of social moments. The conflict is resolved by the separation of exchange value in the form of money. The commodity split into commodity and money.[498] In money is found the external separation of the social moment. *The internal contradiction, splitting the commodity, as a whole, found its resolution in the external opposition C and M, in the form which from now has completed commodity circulation.*

Apropos this Marx says that 'the contradiction of commodity and money is the abstract and general form of all contradictions inherent in the bourgeois mode of labour'.[499] Thus, the relation of C and M is the form of the basic opposition and of all the contradictions between private and social labour. *But as the relation of private and social labour in the form C and M represents itself only different moments of the reified expression of the social relations of production, then, consequently, the value relation C and M is the universal form of the social relations of exchange economy,* taken as a whole.

From the dialectical nature of the relation C and M follows, that their movement is accomplished by mutually penetrating oppositions through constant transition of one pole to another. In its movement C constantly goes to M and back again. The movement both of C and M, as noted above, is the form of the movement of private and social labour. Therefore the transition of private labour into social labour occurs in the form of C and M, that is in the form of the dialectical penetration of the oppositions C and M.

And from this follows the situation that private labour is invisibly social labour, and social labour in its turn contains in itself converted elements of private labour. *The matter, therefore, boils down to the fact that not only bourgeois labour in general has a duality, but also each of its poles.* For only thanks to the duality of these poles the realisation is possible of the unity of oppositions. Precisely therefore, private labour in the moment of its conversion into social labour, uncovers simultaneously both its private and its social character. *This duality of the poles of private and social labour in conditions of natural exchange of products could not be manifested in reified oppositions.* It received the possibility of manifestation only in conditions of commodity circulation, that is conditions opposing separate products to their universal form – the form of money. *Money, thus, is the instrument of the manifestation of the opposition embedded in the commodity and the form*

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[498]'The historical progress and extension of exchanges develops the contrast, latent in commodities, between use-value and value. *The necessity for giving an external expression to this contrast for the purposes of commercial intercourse, urges on the establishment of an independent form of value, and finds no rest until it is once for all satisfied by the differentiation of commodities into commodities and money.* At the same rate, then, as the conversion of products into commodities is being accomplished, so also is the conversion of one special commodity into money' (Marx 1976, p. 181. Our emphasis – S. L.).

[499]Marx 1987, p. 332.

of the manifestation of this opposition.

From all the above it follows logically that in developed exchange society the being of an individual person is wholly the being of that society and vice versa (mutual penetration of oppositions).[500]

And in this relation, *in the extent to which society conditions the manifestation of the social being of the private individual, in such an extent money conditions the social manifestation of private labour.* Because only with the help of money, as universal equivalent, as universal labour, is made possible the inclusion of the continuous stream of private labour into social-general labour. But, including private into social labour, *money thereby includes the separate individual into society, that is links him to a determined social connection*. Because of this integration the unity is carried out of the poles of commodity economy and thereby is carried out the realisation of social-production relations. *The social role of money, thus, boils down to the function of the developer of relations of production.*

Thus, in a commodity society, *money is the organiser of the spontaneous process of exchange of things, and together with this also the organiser of human relations.* In this consist the nature of money from the point of view of its social characteristics.

* * *

As we have seen above, in commodity society, the metabolism C–C cannot be carried out without changes of the form of C. The change of the form of C is its movement with the help of the equivalent of M. But the movement of C is the movement of commodity society, as a whole. In this sense M is the form of movement of commodity society. 'Money acts for the seller of the commodity, as a converted form of C, and the movement of money, as the medium of circulation, is therefore, in fact, merely the movement of commodities while changing their forms', Marx says in this regard.

However, as an independent 'separated' economic category, *money has its own proper, although also dependent on C, movement, and therefore also its own form and content.* A comprehensive definition of the category of money from this side we find in Marx. 'Money, – he says, – emerges as a mere medium of exchange of commodities, not however as a medium of exchange in general, but a medium of exchange adapted to the process of circulation, i.e. a medium of circulation'.[501] From the viewpoint of form money 'is a mere medium of exchange

[500]The individual is contrasted to society, not as part of a whole, but as its opposition, as its polarity. The individual is not only a private person, but at the same time also a social. Therefore his private labour in a hidden state is simultaneously private and social labour. Being disconnected and cut off from society by the private side of his labour, the individual is combined with it by its social side. And this moment of combination is the moment of the manifestation of social labour, the moment connecting the individual with society, a connection which is established with the help of M.

[501]Marx 1987, p. 332.

of commodities'. In this respect, that is from the formal side, it is entirely impossible to distinguish, whether money is only a 'medium of exchange in general', or whether it is a 'medium of circulation'. The difference can only be set when considering the content. From the viewpoint of the content money is a 'medium of exchange, adapted to circulation'. What does this mean? This means that gold circulates in the quality of instrument of exchange for commodities only because it once circulated in the quality of a mere commodity. In this sense gold, like also every other commodity, possesses labour value, and therefore abstract labour is the basic nature of money, the basis of its content. But historically the commodity gold *becomes money only when it on its equivalent-value basis begins to act in the quality of universal measure of commodity values*. Because the first function of commodity-money, which it takes as 'independent' category, is 'to supply commodities with the material for the expression of their values ... The commodity gold thus serves as a universal measure of value. And only by virtue of this function does gold become money'.[502] The question is why the function of measure of value is the first and primary function of money? Because 'money as a measure of value is the necessary form of appearance of the measure of value which is immanent in commodities, namely labour-time'.[503]

The movement of C–C without changes of the form of movement of C, and the change of form without 'manifestation of the measure of value immanent of commodities', cannot be carried out. The movement of C–C exists in the form of M only inasmuch as M is the form of manifestation of the 'immanent to commodities measure of value'. Hence *the social property of gold-money, which distinguishes it from any other commodity, consists of the fact that it is the measure of value*. And from this follows that that commodity, which cannot be the measure of value, can also not be money (true, not every commodity which for whatever reason can act as measure of value, is money, see the above stated on the coalescence of the universal form of value with a determined thing). *In this, different from other commodities, social property of commodity-gold of being measure of value also consists the content of money*. Just as in its coin expression the form of money steps forth.

Herewith, if the form of money expresses itself just an external relation of money token to commodities, then the content of money expresses itself the internal relation of value, contained in the commodity and money. The external relation of money tokens to the commodity world finds its expression in the function of medium of exchange. The internal relation of values, enclosed in money and commodities, finds its expression in the function of measure of value. In the first case the functional side of the category of money steps forth, in

[502]Marx 1976, p. 188.
[503]Ibid.

the second case – the substantial. Only in the unity of the functional and substantial sides (form and content) money displays its nature.

Meanwhile *the quantis limit the nature of money only to the functional side, that is the form*. The substantial side, that is the content of money, is dropped in them. Not understanding the duality of bourgeois labour and its dialectical unity, the quantis mechanically counterpose the moment of production to the moment of the circulation of money. Such contrast leads to an artificial division of these moments. And therefore the means of exchange in the quantis acts as a medium of exchange in general, but not as medium of exchange, 'adapted to circulation', that is as a technical means of exchange of products, but not as converted form of the movement of commodities.

Wherewith the disregard of the function of measure of value does not at all follow, like in the nominalists, from the denial of the substance of value in the monetary material. On the contrary, despite the recognition of the value basis of money, the quantis-classics came to ignore the function of measure of value. Ignoring the substantial side of the category of money was in the quantis-classics not a presupposition, but a consequence of their analysis of money. How could this happen? This happened only because they replaced the content of money with the form, the essence with the phenomenon, the qualitative moment – with the quantitative and reduced money to medium of exchange in general. Reducing money to means of exchange in general, the quantis thus severed the form and content, have eviscerated in money its spirit, turned it into a symbol of commodity values (or commodity prices).

It is interesting in this relation to note the circumstance that the Marxist Hilferding slides to the quantis precisely in that point of his theory of money, *where he begins to interpret the basic function of money – the function of measure of value, where he begins to interpret it in terms of quantity, but not quality*, that is where he starts to substitute the qualitative moment with the quantitative, and hence draws the conclusion on the possibility of unsubstantial moneys also having the capacity of measure of value. So, for example, Hilferding believes that 1) under gold currency, with compliance to the law of proportion of paper moneys relative to gold, they are representatives of gold; 2) under pure paper-money currency (just as under restricted coinage), they are representatives of commodity value and in this sense act as instrument of the measure of value. But Hilferding here only repeats what was before him said by Ricardo.[504]

However paper moneys in conditions of a pure paper currency are representatives of the

[504]Ricardo ['Works, p. 402' reference not found].

value of that real money, which should circulate on the market. For 'the absence of gold – as Livshits correctly says – as circulating money does not at all destroy the objective regulating significance of its value. It continues objectively to serve as measure of value of these [tokens], displaying its value through paper moneys, whose total value it regulates'.[505]

Money stands in a value relation with commodities only because it itself has value. Without value of its own nothing can be a measure of value, nor therefore be money. That is why, for example, in the era of war communism, when in commodity circulation there was no gold, the measure of value became a simple commodity (bread, salt, and so on), and precisely a commodity, as embodiment of social labour, and not some 'pacifier [dummy]', not some 'token'. And in vain Hilferding reproaches Marx for his 'detour' determination of the value of paper money, showing at the same time the 'expediency' of the deduction of this value 'from the socially circulating value'. In so doing Hilferding separates the tokens of value – paper moneys – from gold currency, the counterposition of them directly to the commodity mass, gives them the function of measure of value. But thereby he rolls down entirely to the quantis. The inadmissible error of methodological order is made also by those economists (from the Marxists), like Trachtenberg, Varga and others, who consider the quantity theory of money correct in relation to paper money, but incorrect in relation to full-fledged money. Thereby they accept that tokens of value – paper slips – are also money. But they forget that gold, in the quality of instrument of circulation, also is a 'symbolic money', also is a token of value. Having said A, they should also say B, if they were consequent, that is having accepted the correctness of the quantity theory in relation to symbols – paper slips, they would have had to recognise its correctness also in relation to symbols – metal tokens. That is what, by the way, Livshits did in the question about the purchasing power of money. Having accepted the correctness of the concept of purchasing power of money in relation to tokens of value, he had to extend this concept also to full-fledged money, that is to money in general, but thereby comrade Livshits went over to the quantis (see on this below).

Hilferding nevertheless needs to be done justice. Building his theory of money on the experience of Austrian money circulation, he had to admit that 'a pure paper money, in the final light, must prove impossible', because 'circulation would be subjected to constant disturbances', since there is no possible guarantee that the state will not increase arbitrarily the issue of paper money, since gold is always necessary, as a means of storing wealth in such a form in which it is always available for use, since without gold money one cannot make international settlements, etc. However, denying the possibility of pure paper money

[505]Livshits 1924.

circulation practically, Hilferding admits this possibility theoretically. And in this consists his fundamental methodological error. No doubt this error in Hilferding *follows from an incorrect understanding of commodity-money (its reduction to a simple commodity), and the latter – from an incorrect understanding of abstract labour*. And all this taken together follows from a revisionist guideline on the object of study – exchange economy. Hilferding attempts to revise the basic methodological position of Marx, consisting in the fact that capitalism is governed by spontaneous laws, lying at the basis of simple commodity economy. Hilferding attempts to limit these spontaneous laws by allowing (within certain minima for capitalism) elements of conscious regulation. This he did in relation to pure paper-money currency. 'The social character of money, – says Hilferding, – appears directly here in the regulation of society by the state' (*Finance capital*). However Hilferding forgets that, firstly, 'social regulation of the state' is only the external expression of the regulation of exchange economy by the spontaneous movement of values, and secondly, that this spontaneous movement of value is fundamentally impossible without changes of their forms, that is without the function of measure of value. But, forgetting this, Hilferding in the theory of money safely came to the vulgar understanding of the nature money, which in this relation is exhibited by quantis on one hand, and nominalists – on the other.

Summing up a few results in respect to the determination of the essence of money by the quantis, one can draw the following conclusion.

The quantis understand that money is a commodity, but they do not understand that it is a special kind of commodity, a commodity with a particular social property. They see in it the identity with other commodities, but do not see the existing differences.

The quantis understand that money is a commodity, but they do not understand in what way and why a determined type of commodity on a certain historical level of exchange economy becomes money.

The quantis understand that money is a means of exchange, but they do not understand that it is not just an instrument of exchange, but an instrument of exchange 'adapted to circulation', that is, that it is a form of the movement of commodity values.

The quantis understand that money is a means to facilitate exchange, but they do not understand that circulation of commodities without money fundamentally is impossible, that is, that money is a to commodities immanent means of their circulation (as means of measure of values).

And all this the quantis do not understand because *to them is alien in general the point of view of development, the point of view of the genesis of exchange society, and together with*

this the point of view of the genesis of the category of commodity, the point of view of development through contradictions.

From the aforesaid on the essence of money, from the viewpoint of the Marxist method, the following conclusions derive: 1) The genesis of the bourgeois mode of production is at the same time, the genesis of the commodity, and the genesis of the commodity is at the same time the genesis of money. 2) The existence of money (essence), as unity of the function of measure of value and the function of circulation, is entirely caused by the existence (essence) of the bourgeois mode of production. 3) The essence of the bourgeois mode of production boils down to the fact that individual commodity producers (or capital producers) can realise their own private products of labour only through their inclusion in the general social product, that is to realise them as part of the aggregate social product, – a contradiction that can only be solved with money. 4) *Hence the nature of money consists in the point that it a) is realisation of private labour, including it into social labour, and herewith also the realisation of social relations of production, the inclusion of separate individuals into society; b) that it carries out this realisation in the quality of instrument of measure of value, and c) that money is a measure of value only because it itself possesses value*.

And hence with complete clarity it follows that as long as the bourgeois mode of production exists in its qualitative determination as commodity circulation, which is based on the contradictory movement of oppositions between private and social labour, then there will exist also money in its qualitative determination as measure of value and means of circulation. Until then all attempts to reduce the essence of money to its function of means of circulation, and therefore to value-tokens, will be doomed to complete failure. Because, no matter how high the monopolisation of capitalist production developed, no matter the extent the credit system stepped forth with its 'fictitious' circulation and further restricted gold circulation, all the same, until then, as long as there will no absolute resolution of the opposition between social production and private appropriation, or, what is the same, between private and social labour, until then the capitalist economy will not be able to jump out of its own shell, will not be able to go beyond its own limits – commodity circulation. And in the limits of this circulation there cannot be movement of commodities, without a 'golden spark', without a basis of this movement – the measure of value.

That tokens of value cannot independently fulfil such social functions, as, let us say, the function of measure of value, the function of hoarding, the function of payment, that they in general are not able to fluctuate [function of hoarding], and hence also be a social instrument of the organisation of the mass process, is not only observed during crises and inflationary

periods in the economy, but also in normal times – in international commodity circulation.[506]

As illustration to the stated about tokens of value let us take money, well, at least, in the function of hoarding, and see to what extent this essential function of money can be fulfilled by tokens of value. What is hoarding from the viewpoint of the circulation of M? Treasure is first of all an interruption of the metamorphosis of C–M. But an interruption of the metamorphosis C–M is, in essence, nothing but the transformation of coin into money, because, as Marx says, 'coin itself becomes money as soon as its movement is interrupted'.[507] The money, which in circulation is isolated as coin, as token of value, in treasure once again shows itself, as money: as universal equivalent, as abstract wealth, that is as reification of abstract labour. Consequently, in the function of treasure only full-fledged money can act, that is money in the full sense of the word.

And it is no coincidence that in the quantis the function of treasure entirely falls out of sight or takes a peculiar expression. For example, in Ricardo the function of treasure in his theory is completely absent. For Mill treasure is a completely useless social function of money. In Fisher the concept of treasure is reduced to the slow movement of money in exchange. Generally speaking, for the quantis it is characteristic that they deny the regulating role of treasure of the amount of money in circulation. And all this, of course, is explained by the fact that in the quantis money – is a token of value. It is characteristic for tokens of value, that they, once issued in circulation, will not come back.

The social role of the function of hoarding for Marx boils down to a spontaneous regulation of the circulating monetary mass. Treasure is the reservoir of circulation, in which surpluses of money accumulate and from which are drawn the missing in circulation amount of monetary mass.[508] The role of spontaneous regulator of the amount of the circulating monetary mass cannot be by performed by unsubstantial money, if only already because it under the laws of circulation of value-tokens, once entered into the channels of circulation, will not return.

In the quantis (Ricardo and Fisher) indeed all money goes in circulation, and therefore the function of hoarding in their theory is missing. This circumstance is quite linked with the

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[506]And not for nothing Mill holds that tokens of value can be means of circulation only inside a given country. As concerns international commodity circulation, then it must be provided by full-value money. Here Mill showed that 'ingenious conjecture' in relation to the nature of money, which he nonetheless could not unravel because of a conception of money, as a mere commodity.

[507]Marx 1987, p. 359.

[508]'In order that the mass of money actually in circulation may always correspond to the saturation level of the sphere of circulation, it is necessary that the quantity of gold and silver available in a country to be greater than the quantity required to function as coin. The reserves created by hoarding serve as channels through which money may flow in and out of circulation' (Marx 1976, pp. 231–2.).

conception of money as token of value, but this does not link with factual reality. Tokens of value – are not money, and money – is not a token of value.

In relation to the essence of money the quantity theory does not correspond to the actual situation of things, just as in relation to its conception of exchange economy, which it incorrectly reduces to the natural form of exchange.

The main methodological error of the quantis consists in the fact that they do not recognise the principle variability of exchange economy. And therefore they do not recognise also the historical phases of this economy: 1) direct moneyless trade, 2) simple commodity–money economy, and 3) commodity–capitalist economy, as phases, which differ from each other in several qualitative features. This is on one side. On the other side, the development of exchange economy for them is identical with a simple quantitative growth of natural elements, firstly, as if it were without any fundamental change, and secondly, as if it were without any internal contradiction. For them commodity circulation differs from simple barter not by quality, but only by its quantity, therefore in the main it coincides with it. The introduction in commodity circulation of money does not significantly change anything essential.

Hence the quantis do not understand also the genesis of the bourgeois mode of production, and together with it also the genesis of the commodity, as well as the commodity nature of money. The incomprehension of the essence of money leads some to a distortion, and others to a denial of the substantial side money, and herewith also to the reduction of money to tokens of the value of commodities with all the ensuing errors from this: the dependence of the value of money, as well as the prices of commodities on the amount of monetary material, the denial of (or distortion) of treasure's regulating role of the amount of money in circulation, and so on.

5. So called 'purchasing power of money' in light of Marx's theory of value

Put forward by Hume in his time, and then developed in great detail by Fisher the concept of purchasing power of money, based on the position that commodities enter circulation without price, and money without value, hardly represents itself great methodological interest, since it has as it presupposition the denial in commodities and money of labour value. Much more interest from this side represents the concept of purchasing power of money, developed by Ricardo-Mill and now supported by some Marxists, since it

presupposes a recognition of labour value in commodities and money, and therefore has a close bearing to Marxist political economy. We therefore consider it expedient to focus our attention only on the understanding of purchasing power of money of Ricardo-Mill and some of its present supporters from the Marxists.

The concept of 'purchasing power of money', from the point of view of the quantis-classics, follows directly from the concept of the 'value of money'. 'The value of a thing is what it will exchange for: i.e. the purchasing power of money', – says on this subject Mill.[509] Hence the concept of purchasing power of money must be analysed from the perspective of the value of money in general. Both Ricardo and Mill in the basics similarly understand the value of money and in the basics similarly determine its purchasing power. Therefore in the following we will talk about the value of money of Ricardo-Mill, as a single conception.

Both Ricardo and Mill proceed from the entirely correct presupposition, *the determination of the value, like also the value of any other commodity, by the amount of labour time in its production*,[510] or, as Mill puts it, 'cost of production'. Proceeding from these assumptions, Ricardo in the beginning of his analysis of money makes a series of entirely correct conclusions. In agreement with the developed by him theory of relative value he, for example, considers money, as commodity, to have a determined intrinsic value, measuring the value of other commodities. And further, the amount of means of circulation is determined on the one hand by the value unit of the monetary measure, and on the other, by the sum of exchange values of commodities.[511] Because of this situation mere value-tokens, issued in proportion, determined by the value of money, can replace it in circulation and their value is measured by the value of gold, which they represent. In other words: *the value of money gives the prices of commodities, these tokens of value are tokens of a determined amount of gold, and not lacking substantial value representatives of commodities, as is the case in Hume-Fisher*.

It would seem that Ricardo, on the basis of these methodologically enduring conclusions, drawn by him on the first steps of his analysis, would have had to draw the further conclusion and build the correct scientific theory of money. Ricardo would have had first of all to deduce the function of measure of value and – separately from it – the function of circulation, and herewith develop an independent theory of paper-money circulation. Based on these two functions Ricardo would have had to deduce further the function of hoarding, the function of payment and finally, the function of world money. However this he did not do and with the

[509]Mill 1909, p. 489.
[510]'Gold and silver, like other commodities, have intrinsic value' (Ricardo 1810, p. 1.).
[511]See on this Marx 1987.

task of building a theory of money he does not cope.

The unexpected 'turn to the opposite point of view' Ricardo makes in the question about the relationship between C and M in exchange, in the question, which in him is turned into the question about what the relation of the value of money is to its permanently altering amount. Here Ricardo, like Mill, comes to the conclusion that the value of money is determined not only by 'cost of production', but also by the demand and supply of money, and this, as we shall see, is tantamount to saying that it is determined by the quantity of money found in circulation. This quantity of money can arbitrarily be changed in one direction or another by the appropriate branch of industry (production of gold), as well as by the state (production of banknotes).

The train of thought of Ricardo-Mill in respect to their determination of the value of money, and herewith, also its purchasing power, boils down, first of all, to the following. Commodity circulation – is naturalised exchange. The movement of C in this exchange is accomplished in the form of relative value. M – is a mere commodity, whose use in exchange does not at all alter the in natural exchange existing relation of C. M, consequently, is subject to the same laws of exchange, as every other commodity.

The fundamental law, by which the prices of commodities are established, is the law of demand and supply. This law holds also for money. 'The value or purchasing power of money depends, in the first instance, on demand and supply', says Mill apropos this.[512] The law of demand and supply, in this way, establishes: for commodities – the price, for money – the purchasing power. The purchasing power of money – that is its price. The value of money, the purchasing power, the price of money, in this way, – are identical concepts.

But price is the realisation of value. It is above or below its labour content. The purchasing power of money is therefore the realisation in circulation of the value of production and is above or below its labour content. In other words, *the classics establish for money two types of value: the value in production and the value in circulation*.[513]

However, 'the demand for money consists of all the goods offered for sale', and the opposite: 'the whole of the money constitutes the demand for goods'.[514] Therefore *both the prices of commodities and the purchasing power of money is the result of the relation of two magnitudes, two independent currents*: the money and the commodity mass, found in any given moment in one or the other country, or a set of countries, involved in world trade, in

[512]Mill 1909, p. 490.
[513]'Money is a commodity, and its value is determined like that of other commodities, temporarily by demand and supply, permanently and on the average by cost of production' (Mill 1909, p. 488).
[514]Mill 1909, p. 491.

circulation. *Prices of commodities determine the purchasing power of money, and the purchasing power of money – the prices of commodities*. One and the other get their expression by actual exchange.

With this, since prices of commodities before circulation are not determined, the demand for M from the side of C is not limited, while the supply of M is always limited, because 'there is always a demand for as much money as can be got'.[515] From this follows that the decisive factor is the supply of M, that is its quantity. But this means that the quantity of M determines its value, and with it also the prices of commodities. 'The value of money, – Mill says, – other things being the same, varies inversely as its quantity ... The whole of the goods being in any case exchanged for the whole of the money which comes into the market to be laid out, they will sell for less or more of it, exactly according as less or more is brought'.[516] In the same spirit also Ricardo speaks: 'Commodities rise in prices proportionally to the higher or lower quantity of money'.

Thus, it was sufficient for the classics to take as starting point such a supposition, that M is an ordinary commodity, but nothing more, since they inevitably came to the conclusion in the spirit of the quantity theory, namely, that *the value of money, and with it also the prices of commodities is determined by the quantity of the money material, found in circulation*.

True, Mill, in his understanding of money circulation, stands significantly closer to the truth than Ricardo. He more precisely poses the fundamental question, the question about the inter relation between C and M and more correctly solves it. He is the first to pose the question, 'whether the amount of money in circulation is determined by the prices of commodities, or the prices of commodities determined by the amount of money in circulation'.[517] And if he did not solve this question, then, in any case, he made some correct conclusions. So, for example, if Ricardo believed, that in circulation takes part the whole amount of money material, found in a country,[518] then Mill, on the contrary, viewed that 'whatever may be the quantity of money in the country, only that part of it will affect prices which goes into the market of commodities, and is there actually exchanged against goods'.[519] In other words, for Mill, circulation of one or other country can absorb only a determined quantity of means of circulation. If to this is added still more and that 'the market price of a commodity is determined by the complicated operations of demand and

[515]Mill 1909, p. 490.
[516]Mill 1909, p. 493.
[517]Marx 1987, p. 396.
[518]In this relation Ricardo departs with Hume, who mechanically counterposes all money tokens of a country to all commodities, present on the market.
[519]Mill 1909, p. 496.

competition, which are quite independent of the quantity of gold and silver in the country',[520] then is shown that Mill went nearly to the truth. There remained for him only to make the final conclusion, namely, that the quantity of M in circulation is determined by the prices of commodities, and therefore entirely and fully due to the demands of commodity circulation. But he could not draw this conclusion, since he started from a false supposition, that is that M itself is an ordinary commodity and that the movement of M is independent from the movement of C. Likewise Mill closely went to the question about the role of hoards, as regulator of the required amount of money in circulation. But also this question he could not solve correctly, starting from the same supposition that M is an ordinary commodity.

And therefore, although the quantity of money for Mill also is determined by commodity circulation and the ultimate 'regulator is cost of production', nevertheless 'the quantity of money inevitably must influence on its value',[521] and its value – on the prices of commodities. And since prices of commodities are determined only in circulation in the result of the inter relation of the market value of money and commodities, and since they mutually condition each other, then the opposite: the prices of commodities influence on the purchasing power of money, and finally on its quantity.[522] However, contrary to the opinion of Mill, the average price and prices of commodities are not one and the same. The average price is a fact of production. The amount of money in fact is determined by the prices of commodities, expressed in ideal value money, and not average price, expressed in purchasing power of money tokens.

In this way, regardless of some differences of the theory of circulation of money of Mill from the theory of Ricardo, fundamentally their final conclusions coincide.

The central thought of Ricardo in the domain of the theory of money circulation boils down to the following. Between the metallic value of gold and its value as instrument of circulation, due to a certain kind of incoherent mechanism of commodity circulation, there is established a contradiction. The value of money in circulation is constantly deviating from its labour content. However, this contradiction is eliminated by counter-posing movements upward and downward of the values of commodities and the value of money, by movements, resulting in the process of price-formation. The conflict finds its resolution in the price level, and its expression in the purchasing power of money. According to this process of price-

[520]Mill, cited by Marx 1987, p. 397.

[521]Mill 1909, p. ~505.

[522]'The prices of things will, on the average, be such that money will exchange for its own cost in all other goods: and, precisely because the quantity cannot be prevented from affecting the value, the quantity itself will (by a sort of self-acting machinery) be kept at the amount consistent with that standard of prices—at the amount necessary for performing, at those prices, all the business required of it' (Mill 1909, p. 505).

formation Ricardo establishes a peculiar mechanism, regulating the value of money.[523]
Formally the mechanism of this regulation is expressed:
1. *For international commodity circulation* – in constant adaptation of gold to its course, that is in a constant effort to maintain the same proportion between the commodity and monetary masses of different countries.
2. *For internal commodity circulation* – in the adaptation of gold producers (or bank production of banknotes) to the demand for the monetary commodity, that is expressed in the expansion and contraction of production of the monetary material.
In essence this mechanism of regulation of the value of money (both for domestic and international circulation) boils down to the point that a constantly occurring deviation of the value of gold in circulation, as a consequence of market forces, in the end still is regulated by the labour content of its production.[524] But in Ricardo it turns out that, regulating its own value, money thereby regulates the prices of commodities, being, thus, an active price forming factor.
The mechanism of price formation, and herewith also the mechanism of the regulation of the value of money, can be schematically represented in following way. Let us take Ricardo's position of departure, which consists in the point that '*if the value of gold is given, the amount of money in circulation is determined by the prices of commodities*'.[525] Based on this methodologically indisputable position, let us make in the spirit of Ricardo's reasoning

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[523]The presentation of the mechanism of price formation and the value of money is made after Marx. See Marx 1987, pp. 402–7.
[524]Ricardo - 'If in the progress towards wealth, one nation advanced more rapidly than the others, that nation would require and obtain a greater proportion of the money of the world. Its commerce, its commodities, and its payments, would increase, and the general currency of the world would be divided according to the new proportions'.
'The equilibrium between that and other nations would only be restored by the exportation of part of the coin'.
But 'no person ever exports or imports bullion without first considering the rate of exchange. It is by the rate of exchange that he discovers the relative value of bullion in the two countries between which it is estimated'. And further: 'The money of a particular country is divided amongst its different provinces by the same rules as the money of the world is divided amongst the different nations of which it is composed'.
At the basis of this redistribution of the monetary mass lies the law of demand and supply, which regulates the production of monetary material and therefore also its value: 'If a mine of gold were discovered in either of these countries, the currency of that country would be lowered in value in consequence of the increased quantity of the precious metals brought into circulation ... Gold and silver, whether in coin or in bullion, obeying the law which regulates all other commodities (the law of demand and supply. – S.L.), would immediately become articles of exportation'.
But – 'If instead of a mine being discovered in any country, a bank were established, such as the Bank of England, with the power of issuing its notes for a circulating medium; after a large amount had been issued ... the same effect would follow as in the case of the mine. The circulating medium would be lowered in value, and goods would experience a proportionate rise. The equilibrium between that and other nations would only be restored by the exportation of part of the coin'.
Likewise also the equilibrium between individual regions of a given country would be restored through reducing production of the money commodity.
(Ricardo 1810, pp. 4, 26.).
[525]Marx 1987, p. 402.

the assumption:

1. *The sum of exchange values of commodities decreases* – a) due to production of a lesser amount of commodities at the same value, b) due to an increase of productivity of labour, when the same mass of commodities contains less exchange value.

2. *The sum of exchange values increases*: a) when: with unchanged production costs the mass of commodities increases, b) when: because of increase of productivity of labour its amount increases.

Question: what becomes of the given amount of circulating metal? If one proceeds further from another assumption of Ricardo, namely *that 'gold is money only because it circulates as a medium of circulation, and if it is forced to stay in the sphere of circulation, like paper money with forced currency issued by the State*'.[526]

Then: in the first case – the amount of money will be higher in relation to the exchange value of the metal; in the second – lower.

Hence: a) also in the first case gold would be a token of a measure with lower value, than its own, and b) with the second – a token of a measure with higher value.

And this means: a) in the first case gold, as a token of value, will be constantly below; b) in the second – constantly above its intrinsic value.

In other words: a) in the first case happens the same as if commodities would be assessed by a measure of a lower; b) in the second – of a higher value.

Therefore: a) in the first case the price of commodities would increase; b) in the second – fall.

But: '*The movement of commodity prices, their rise or fall, in either case would be due to the relative expansion or contraction in the amount of gold in circulation occasioning a rise above or a fall below the level corresponding to its own value; i.e. the normal quantity determined by the relation between its own value and the value of the commodities which are to be circulated*'.[527]

In other words: the value of money in circulation fluctuates around its internal value; with what commodities are measured is not this internal value of the monetary material, but that value of money in circulation, that is the purchasing power of money. But this at once also means, that commodities come into circulation without price, and money – without value. Because, whatever the 'regulatory action' of the internal value of money on its outward value, that is value in circulation, it remains an undeniable fact that for Ricardo it has no direct relation to the prices of commodities and also is not a measure of value. *The measure of value turns out to be the value of money, or so called 'purchasing power', which it*

[526]Marx 1987, p. 402; our emphasis - S.L.
[527]Marx 1987, p. 403; our emphasis. – S.L.

supposedly gets in circulation. If we further consider that money in the quality of instrument of circulation acts in the form of tokens of value, then for Ricardo is obtained, that tokens of value may be a measure of value of commodities. It was in this point, as we saw above, that Hilferding comes to Ricardo, but... departs from Marx.

* * *

The fateful question for Ricardo-Mill is undoubtedly the question of the interrelation of C and M. Starting from the methodological assumption that *commodity circulation is identical to direct exchange, they believe, that M is a simple commodity, and its movement is identical to the movement of C*. But Ricardo-Mill, as was already shown above, leave out of sight the fact that commodity circulation is fundamentally different from direct exchange, and therefore also the relation C–M, as commodities (in commodity circulation), is only formally identical with the relation of mere commodities (in direct exchange), but in essence deeply differs from it. Together with this the quantis 'do not see that gold, as a mere commodity, is not "yet" money',[528] just as money, considered in conditions of commodity circulation simply as gold, 'already' is not a mere commodity, but a commodity with a special property. Money includes both of these moments: both the fact that gold is a mere commodity, and also that gold is more than a mere commodity. The duality of commodity – gold: as mere commodity and as commodity–money, on the one hand, is an expression of the duality of bourgeois labour in general, on the other hand, – is itself expressed in the duality of the exchange relation of C and M. In other words, the relation of C and M, on the one hand, is a mere commodity relation (and in this sense, their exchange value is expressed in the form of relative value),[529] on the other hand – that relation of polarised commodities where M acts as 'alienated shape of all other commodities',[530] as universal equivalent and universal measure of values, that is as converted form of the movement of C[531] (and in this sense exchange values of C and M are expressed in the universal form of value, that is in the form of absolute value).

For the quantis-classics there exist only the simple relative form of value, and with that also the simple exchange relation C and M. For them it is unclear that in money we have the modification of relative into absolute value.

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[528]Marx 1976 , 199 p.

[529]'Money, like every other commodity, cannot express the magnitude of its value except relatively in other commodities ... This establishing of its relative value occurs at the source of its production by means of barter' (Marx 1976, p. 186).

[530]Marx 1976, p. 205.

[531]The duality of the relation C and M itself reveals, that *commodity circulation does not abolish simple exchange relations, but includes them in its system of movement, at with it preserves these relations for C and M, but not for C–C.* Because of the monetary form of value the relation C–C acts only in the form of absolute value, but the relation C and M acts both in the relative and in the absolute form of value.

Meanwhile, from the position that M is not a simple commodity, but in the quality of universal measure of value is a converted form of commodity, follows a different position, which in a radical way changes the matter. From this position logically follows that the movement of M derives from the movement of C and that M in its interaction with C plays a passive, rather than an active role.[532]

If this position unrolls logically, then we get entirely other conclusions, than the classics made.

Firstly. If C and M are taken from the viewpoint that they are only mere commodities, then between them are established simple exchange relations, relations of direct exchange. These relations exist in the exchange of commodities for gold at the source of its production.[533] Here, as a result of the law of simple exchange (the interplay of labour content of value and demand–supply) is established the price of commodities and the [relative] value of money. 'This relation, however, may express both the magnitude of value of the commodity and the greater or lesser quantity of money for which it can be sold under the given circumstances'.[534] In the same way in this exchange relation the magnitude of the [relative] value of money is established, as well as that plus or minus compared to it, which accompanies the alienation of money under the given circumstances of direct exchange.

'But from that moment onwards, it (gold – S.L.) always represents the realized price of some commodity'.[535] In other words, *the prices of commodities, as well as the value of money are established before circulation*. In circulation only the prices of commodities are realised, and the value of gold only 'expresses these realised prices'. And if in the process of circulation, by force of a whole series of spontaneous causes the prices of commodities significantly deviate both from their labour content, and from the expression which they got in money in the process of direct exchange at the source of gold production, then gold already does not suffer these deviations in circulation. And gold does not undergo these deviations, not only because 'the value of gold is already given in the prices of commodities[536] 'or that when gold 'enters into circulation as money, its value is already given',[537] but also because *the role of gold in the interrelation of C and M is entirely other*

[532]In Ricardo-Mill both C and M play a similar active role: they at the same time condition each other and mutually determine. Between them exists only an antagonism, but not a unity of oppositions, where the stress [*privus*] should remain on C.

[533]'In order to function as money, gold must of course enter the market at some point or other. This point is to be found at its source of production, where the gold is exchanged, as the immediate product of labour, for some other product of equal value' (Marx 1976, p. 204).

[534]Marx 1976, p. 196.

[535]Marx 1976, p. 204.

[536]Marx 1987, p. 327.

[537]Marx 1976, p. 186.

than the role of commodities.

> But for what is the commodity exchanged? For the shape assumed by its own value, for the universal equivalent. And for what is the gold exchanged? For a particular form of its own use-value.[538]

Herewith, if commodities express their own value in ideal gold, as universal equivalent, and their prices can fluctuate around that ideal value of money, as around its own, then money expresses foreign value with its own 'ideal' value. Precisely in this 'ideality', as absolute expression of commodity value, consists the essence of money as the universal measure of value. The function of ideal (full-fledged) gold – is to realise the ideal prices of commodities. And it is not its (gold's) 'fault', if commodities in the market will be 'realised' above or below their ideal prices, expressed in the value of money. The value of money itself from this does not undergo any own change, since in circulation it already does not act in direct relation with commodities. Change of the value of money can only happen as a result of a corresponding change in the very production of gold.

That is precisely why, if one can still speak about possible deviations of the exchange value of gold from its labour content in the conditions of direct exchange at the sources of production, then to speak about deviation of the value of money in circulation is not allowed in any case. Factually this has no place. On the contrary, a constant value of money takes place in circulation. The exchange value of gold is established in direct exchange at the sources of production and enters circulation, as a given and immutable magnitude.

Secondly. Once prices of commodities are given before circulation and once the velocity of metamorphosis is certain in circulation, then thereby is given also the amount of M, which should itself serve the function of medium of circulation. The amount of money, thus, is not an arbitrarily given magnitude, as is presented by the pure quantis and as this, albeit with a different formulation of the problem, is presented by Ricardo, but is conditionally derived, because 'money is only the representation in real life of the quantity of gold previously expressed in the imagination by the sum of the prices of the commodities'.[539]

And if it is so, then it goes without saying, that the amount of money cannot in any way affect the prices of commodities. It can likewise neither extend influence on its own value because under free coinage, in conditions of a gold currency, this amount is regulated by treasure. The value of money is regulated by 'cost of production' not 'in the final light', as Mill claims,

[538]Marx 1976, p. 213.
[539]Marx 1976, p. 203.

but directly, through adaptation of the gold industry to the other branches of production. Another regulator for the value of money there is not and cannot be. And therefore there is also not a sort of particular purchasing power of money besides the intrinsic value, expressed with ideal gold. Therefore, there is not any necessity to use this concept in the theory of circulation, as an independent category, because it coincides with the notion of measure of value.

Perhaps, it would be legitimate to still speak about purchasing power of worthless money – tokens of value. But tokens of value – are not money, just as money – is not a token of value. Tokens of value are completely controlled by other laws of circulation, than substantial money, and their circulation is a derivative from the circulation of the latter. Therefore to build the concept of purchasing power of money on the basis of the law of circulation of tokens of value and apply this concept to money in general – is at the least misleading.

Thus also the problem of purchasing power of money is decided not in favour of the quantis. As in the question about the nature of money, so also in the question about its purchasing power (value of money) the errors of the quantity theory are due to the same methodological presuppositions: by reducing commodity circulation to direct exchange, and money – to a mere commodity, and by a wrong understanding of abstract labour, in view of the incomprehension of the duality of bourgeois labour.

But if these methodological flaws in a significant degree are extenuated for the classics, then they not in any way can be extenuated for Marxists.

* * *

Meanwhile we have among us Marxists the formation of a whole direction, which believes, that form the Marxist essence of money the concept follows of purchasing power of money, which finds its confirmation in the practice of monetary circulation.

Insofar as we know, the first who contrived about this is Trachtenberg.[540] He developed a peculiar theory of value of the various forms of money, out of which logically follows that money in the quality of medium of circulation has its special value and, therefore, also special purchasing power. His example proved to be contagious. Along with Trachtenberg, with the him typical methodological carelessness Lubimov contrived about the category money. Recently in their work Livshits and Kon developed a whole system of views, justifying the concept of purchasing power of money in conditions of commodity circulation. We believe it is necessary to dwell only on the views of Livshits and Kon [1897–1941], developed by them: by the first – in the pages of *Under the Banner of Marxism* No. 8-9 in

[540][Trachtenberg 1918. This book is criticised in Berkovsky 1930a, pp. 26–47.]

1924, by the second – in *Course of political economy*, vol. I [1928] and the response to the review of Abezgauz [1900–37], Dukor [1900–38] and Notkin [1901–82] – in the journal *Vestnik* No. 25 in 1928.[541]

Livshits starts from the premise that in the measure of value we have an 'ideal' expression of value, whereas in the means of circulation – a 'real' or, as he puts it, 'reified manifestation of value'. In other words: ideal value, existing in the measure of value finds its real manifestation in real value, existing in money, as instrument of circulation.[542]

Transferring the analogy of the prices of commodities to the category of money, Livshits concludes that if in the process of circulation the form of manifestation of the value of commodities is price, then in relation to money – the form of manifestation of value is the token of value. Hence for Livshits, if the price of a commodity is the 'monetary expression' of the value of a commodity, then the token of value is the 'commodity expression' of the value of money. Herewith both the monetary expression of value of commodities, as well as the commodity expression of the value of money – both of these 'expressions' are displayed factually in the process of circulation. Before circulation we have only an ideal value of commodities and likewise value of money.

At the source of production. | *In circulation.*

1. Value of commodity | Price – monetary expression of the value of the commodity.
2. Value of money | Tokens of value – commodity expression of the value of M.

And further, similar to how the price of a commodity is set as a result of supply and demand, in the same way also the purchasing power of money is set by supply and demand. And therefore the amount of money affects its purchasing power, and the reverse – purchasing power affects accordingly its amount.

With those Marxists, whose concept of 'purchasing power of money' is reduced simply to its value, Livshits does not agree, for the trivial reason that in the practice of monetary circulation there takes place, 'a deviation, even if also temporary, of the purchasing power of gold coins (under the influence of changes of their outstanding amount) from their value, as

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[541][Kon was also criticised in Berkovsky 1930a.]

[542]'Insofar as an instrument of circulation displays [manifests] the "commodity price" of money, it is by itself clear, that the purchasing ability of the money token, serving as this instrument of circulation, is determined not only by the value of the money material which serves as the measure of value, but also by the "conjunctural" commodity market (the mechanism of demand and supply in relation to money)' (Livshits 1924, p. 232).

And regardless of the fact that Livshits criticises Trachtenberg for his treatment of the value of money, according to which it turns out that all forms of money have value, Livshits himself rolls to the recognition of a special value in the instrument of circulation.

measure, resulting in an overflow of gold coins into bullion, and back'[543] (Speaking of gold coins, Livshits, thus, under the tokens of value means simply substantial money, but not tokens of value in the proper sense). From a similar kind of conception of purchasing power of money in Livshits is formed a peculiar understanding of treasure, which in him boils down to a means of regulating the amount of money not through the measure of value, not through 'full-bodied gold' directly, but through the deviation of the purchasing power of money from ideal value, that is through the purchasing power of money. Hence the notable hypothetical example of Livshits about indemnity [*kontributsii*].

Similar to Livshits, Kon too for money establishes the category of purchasing power or the category of price. But if Livshits, at least formally, 'restricts' the concept of purchasing power of money to tokens of value, then Kon operates in a more direct way, and calls things by their right names.

For Kon there exists an ideal price of commodities and an ideal price of gold – on the one hand, a real price of commodities, and likewise a real price of gold – on the other. The ideal value of commodities and money are established before circulation, the real – in circulation. Wherewith before circulation commodities 'only' *are equated* to a determined amount of gold, in circulation they – 'factually' *are exchanged*. This actual exchange also is the first direct exchange, in which commodities and money act between themselves in a real relation. In actual exchange there takes place a deviation of the real from the ideal prices of commodities, as well as the real from the ideal value of gold. Real gold is also the purchasing power of money, or the value of money, expressed with real gold. But since the real price of commodities expresses its value in real, and not ideal gold, then the purchasing power of money is not expressed in the ideal, but in the real price of commodities. Since on the market, in the circulation process, commodities first entered into a real relation with money, then precisely here is established the real relation of C and M. What is from this obtained? Commodities realise their value under actual exchange for real gold. Gold realises its value in its actual exchange for real prices of commodities. But after all the real price of commodity and the real price of gold, from the viewpoint of this 'real' (read direct) exchange – this is nothing other, than the expression of the relative value of C and M, which Kon *volens nolens*, in the wake of Livshits, extracts from the first stage of the exchange process and transfers it to the second stage – in commodity circulation.

For the purpose of methodological criticism there is no need to expose with a more detailed analysis the views on this question of comrade Kon. Also the given is sufficient in order to

[543]Livshits 1924, p. 233.

draw the necessary conclusions.

Kon, similar to Livshits, introduces the concept of purchasing power of money, as a special category for the medium of circulation, thereby gives money the category of price. But thereby he emancipates M in front of all other commodities. Simply put, like Ricardo-Mill, Kon reduces money to a simple commodity.

The difference between Kon-Livshits, on the one hand, and Ricardo-Mill – on the other, consists only of the point that if in the latter commodity circulation was identified with direct exchange, then in the first the direct exchange, existing between C and M at the source of production of gold, is attempted to be identified with commodity circulation. In one of the seminars on political economy (at RANION Institute of economy) Livshits, in the quality of head of seminar, developed the idea that the specific conditions of production of gold are such, that already at its source gold acts as M, because, he said, there is no need talk about a two-stage process of the exchange of gold-money. There is, he said, only the actual exchange in circulation. The same idea develops also Kon in his reply to the review of Abezgauz, Dukor and Notkin, where he says, that before circulation there exists only the ideal equation C and M, but not their exchange.

Hence in him the peculiar understanding of 'ideal price of commodities' and 'ideal gold'. These 'idealities' in Kon are converted in somehow epistemological concepts. Hence also the conclusion that real exchange – is actual exchange, that is direct exchange.

The entire line of reasoning on this subject of Kon-Livshits boils down to the point that they simply slur over that basic methodological position of the Marxist theory of money, which states that a direct exchange of commodity and money, in which is established both the price and value, exists only in direct commodity exchange at the sources of production and that 'from that moment onwards – as Marx says, – money always represents the realized price of some commodity'.[544] Livshits and Kon forget, that *in commodity circulation the element of direct exchange acts already in the quality of surpassed moment*. Here already is finished the relation C and M, as commodities, here begins the relation C and M, as commodity and money. Here M acts in the quality of converted form C, in the quality of absolute and unchanging value. Here happens not the realisation of the relation C and M, as commodity, but the realisation of the relation C–C, through equation to M, as universal equivalent. Therefore if here also happens a deviation of value C from its absolute expression in M, then M itself remains unchanged. It remains unchanged, we repeat, because it acts not in direct relationship with C. But, forgetting all this, Livshits and Kon inevitably roll to the quantis in

[544]Marx 1976, p. 204.

the main question of the problem of circulation, in the question about the amount of money, necessary for circulation.

In short, with the criticism of the viewpoint of Kon-Livshits we come to repeat all the arguments which we used in relation to the viewpoint of Ricardo-Mill. Not to regard other problems, connected with the concept of purchasing power of money (the problem of treasure, and so on), we refer to the readers to an interesting discussion on this topic, unfolding in *Vestnik*, between Kon, on the one hand, and Abezgaus, Notkin, Dukor – on the other.

There is no doubt that in the persons of Livshits-Kon, we have advocates of the long ago refuted theory of the circulation of money of the quantis-classics, but now resurrected by some eclectics in political economy (Katzenelenbaum and others).

That, about which Livshits and Kon speak in their work in relation to purchasing power of money has not any relation with money, as such. All of this has relation to tokens of value. And that question would have had to be considered by them from the standpoint of the theory of the circulation of tokens of value, but not from the standpoint of money as such.

Chapter Twenty-Two

Currency Parity and the Balance of Payments (Contribution to the Critique of the Latest Political Economy)[545]

(1924)

Aleksandr Finn-Enotaevsky

> I haven't yet got round to it, but some time I really must investigate the relation between the rate of exchange and bullion. The role played by money as such in determining the bank rate and the money market is something striking and quite antagonistic to all laws of political economy.[546]

1.

In his review of the manuscript of McCulloch on 'foreign exchange', – which came to light only in 1895, – Ricardo in 1819 wrote:

> In the article on Foreign Exchange, you say, "the price of foreign bills depends on the value of the currency at the place where they are made payable, compared with the value of currency, at the place where they are drawn;" But soon after it is said "that the comparative value of the currencies of particular countries must depend 1st on the relative value of bullion in those countries and 2dly on the quantity of bullion contained in their coins, or on the quantity of bullion for which their paper money, or other circulating media, will exchange." Do you not then mean to say that the price of Foreign bills depends on the relative value of bullion in the countries between which they are negotiated? Under some circumstances you agree with me that bullion might possess a higher value (*relative* value. A. F.-E.) in Poland, than in England, but a bill on France for 10000 francs would not vary in either of those countries on that account,—the same quantity of bullion must be paid in both for the bill on France, without any regard to the quantity of corn or labour that can be commanded by it. ... I cannot help thinking that the language of the Bullion Report is correct ...[547]

When we turn to the *Bullion Report* we find:

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[545]Written March 1924. [This is part of an anthology edited by Finn.]
[546]Letter 23 April 1857 of Marx to Engels. Marx 1983, p. 126.
[547]Ricardo 1895, pp. 37–8.

> The par of exchange between two countries is that sum of the currency of either of the two which, in point of intrinsic value, is precisely equal to a given sum of the currency of the other; that is, contains precisely an equal weight of gold or silver of the same fineness.[548]

Let us emphasise: according to Ricardo the *value* of money metal (let us say gold) in normal conditions is the *same* in different countries; the parity of the exchange rate is determined by the weight of the metal in the money of the different countries; the relative value of money (to *commodities*) here has no relevance. This *basic* position Ricardo keeps also in his *Principles*.[549] According to McCulloch the definition of parity, given in the *Bullion Report*, is wrong. Value of money metal is *different* in different countries. The price of foreign exchange is determined by: 1) the ratio of the value (– relative! A. F.-E.) of the means of circulation in the two countries, and 2) the relative demand and supply on the foreign exchange market.[550]
Let us fast forward a hundred years from this correspondence.

> The main result (obtained in the study of the rich material presented by the world war. A. F.-E.) is, that the exchange rate between two countries with paper currency is determined by the ratio between the value of money in the one and the other country. Since this value of money is measured by the purchasing power of the money within a given country, we can say that this essential determining basis of the exchange rate lies in the ratio between the internal purchasing power of money of one country and that of the other. This ratio represents the equilibrium of the exchange rate and can fittingly be called the purchasing power parity between the two countries ... This result holds true also for the case of gold currency ...[551]

There was necessary, thus, in the second decade of the twentieth century a world war, creating a flood of paper money, for the most distinguished European economist, as the

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[548]Select committee on the high price of gold bullion 1810, p. 22.
[549]'When each country has precisely the quantity of money which it ought to have, money will not indeed be of the same value (relative A. F.-E.) in each; for with respect to many commodities it may differ 5, 10, or 20 per cent, but the *exchange will* be at par. ... In speaking of the exchange and comparative value of money in different countries, we *must not in the least* refer to the value of money estimated in commodities, in either country' (see Ricardo 1821, p. 158. Emphasis by us. A. F.-E.).
[550]Ricardo, on the basis of his quantity theory, reduced in McCulloch the two reasons to one, namely to the first, but in this we are here not interested.
[551]Cassel 1921b, pp. 579–80.

English certify Gustav Cassel, to announce the discovery of a theory of exchange rate, which still in the second decade of the nineteenth century was advocated in one or another form by an 'incredible cobbler', as irreverently spoke about McCulloch his contemporaries.[552]

For us, however, it is not important here, who discovered the now dominant in different variations theory of exchange rate on the basis of the purchasing power of money, but whether it is true. Cassel is considered the most authoritative of its representatives; to him we also will pay the main attention.

For all the similarities between Cassel and McCulloch in the given question, there exists also a fundamental difference between them. McCulloch is a bullionist, Cassel is a tabularist.[553]

An analysis of the latest theory of money is not included however in the task of the present article, yet we have to touch Cassel's – yes and also many other money theories – insofar, as this is necessary for the consideration of the question on exchange rate.

Cassel rejects the category of value, but unlike the ordinary 'empiricists' – their breed is many also among us [in Russia] – he understands, that the operation of a simple replacement of the concept of value 'when it concerns goods and services by the more accurate concept of price' does not pass when it concerns money: because prices are measured in money units. Therefore one needs a workaround.

> The value of money of a given country, he argues, is obviously determined by the mass of the goods or services that you can get for this money. The money unit represents a more or less number of utilities [use values], regardless of how low or high prices are ... A falling value of money is expressed, as a general uplift of prices. We must therefore determine the value of money, as a reciprocal (mutual) value of the general price level ...

Does all this hold true?

If you put in Cassel instead of the value of money the *relative* value of it to commodities, then the assertion, that money, the general commodity equivalent, expresses its exchange value in the *use-value*, utilities, of an infinite number of commodities, would be right and would be consistent with what the 'scholastic' – in Cassel's opinion – Marx says. But Cassel, talking about the value of money, makes a *salto mortale*: from *useful* commodities he jumps to their

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[552][Marx 1989b, p. 370.]

[553]This is the same thing as 'indexist', since the 'tabular standard' is the ancestor of the contemporary index of commodity prices, promoted a good hundred years ago as replacement of the precious metal on the throne of measure of value. One does not need to be a prophet, to predict, that of the idea of a replacement in capitalist economy of the 'barbarous' gold measure by a 'scientific' one, nothing will come also in the twentieth century, despite the fact that [the American] Irving Fisher has a lot of admirers in the old world ...

prices, and it turns out, that the value of money is expressed in a commodity index. It is entirely clear, that by such head-spinning path he determines the value of money in the end by the value of that same money. Under the identification of the value of money with relative value, and naming the latter purchasing power, it of course does not cost anything to say, that the exchange rate is determined by the ratio of the purchasing power of money in different countries.

The resolute nominalist rejects the *own* value of money and directly says, that the purchasing power of money *is not* the value of money, but the price of commodities, that can be bought for money; in prices of commodities there is not the value of money. Such is Bendixen.[554] Cassel first reduced the value of money to the index of prices and announced, that 'the whole theory of the value of money reduces itself to a theory of the changes of the general price level';[555] then he reduced the change of commodity prices to a change in the purchasing power of money, and finally, he reduced a change in the purchasing power of money to a change of its quantity. In this way he safely led us to the bosom of the quantity theory. The latter also brings him to Ricardo. Based on his erroneous quantity theory, Ricardo says, that 'relative prices (of commodities) are determined by the value or quantity of currencies'.[556] And although holding this theory of money, he strongly emphasises that the reason for changes in commodity prices lies in changes in the value of money, due to its quantity above or below the level defined by its intrinsic value and the value of commodities, nevertheless the *tautology* turned by him *into a causal* connection – a rise of commodity prices and a decrease of relative value of money, compared with commodities, are *different* expressions of one and the same phenomenon (Marx) – also avenges itself, in that his theory of exchange rate is equated to the one of Cassel.[557]

'The remaining merit of the classics and especially Ricardo is that they fundamentally established, that the level of prices within the country is determinative for the height of the exchange rate' – says Hahn;[558] and he is not alone. And this in glaring contradiction to the *basic* Ricardian position, that the exchange rate rests on the *value* of money (in relation to the metal) *without any connection with commodities prices*.

> When you speak afterwards of the “difference between the value of the precious metals in the home and foreign market,” in what do you estimate that value? If you say

[554]Bendixen 1912, pp. 31–4.
[555]Cassel 1921b, p. 395.
[556]Ricardo 1895, p. 36.
[557]Among us this can be seen by the example of professor Sokolov: see his 1923 book on p. 264 and others.
[558]See his article [in Finn's anthology]; the same also in his book (Hahn 2015).

> in goods, I ask in the goods of which country?[559]

How actual also today the question is! Cassel, comparing his purchasing power of money, just as McCulloch determines his 'value' of money by its commodity prices in *every* country. Hawtrey, who shares the variation of Pigou, says, that 'for the purpose of comparing the purchasing power of two monetary units, the value of each of the foreign trade commodities must be taken in the country from which it is exported'.[560] And all this for the determination of the exchange rate is untrue. The correct answer is given by Ricardo himself in his *Principles*:

> It may also be ascertained by comparing it with some standard *common* to both countries. If a bill on England for £ 100, will purchase the same quantity of goods *in France or Spain*, that a bill on Hamburg for the same sum will do, the exchange between Hamburg and England is at par; but if a bill on England for £ 130, will purchase no more than a bill on Hamburg for £ 100, the exchange is 30 per cent. against England.[561]

Here Ricardo is in all his logical force: the *common* measure of *value* of money in two countries – is determined by the quantity of *use* values of commodities of a *third* country.

2.

The parity of the exchange rate is determined by the ratio of the *value* of money in the compared countries, the measured value of the *represented* by them metal, now gold. But how is established the value of the precious metal? It corresponds to the price of its production – at best or worst conditions or an average price of production, this depends on the conjuncture of the gold market. From the mining sites gold enters *world* circulation, as *commodity*, before it comes into *national* circulation. This knows also MacLeod.[562] Any change in cost of production of gold is reflected directly everywhere in the world market on its value. The latter on the *world* market, in *international* relations, *depends not* on the *quantity* of it in each different *national* circulation. Gold and silver come into national

[559]Ricardo 1895, p. 39.
[560]See Hawtrey 1923, p. 70.
[561]Ricardo 1821, p. 159 p. Emphasis added. A. F.-E.
[562]Macleod 1894, pp. 677–8.

circulation with already given magnitude of value. (Marx).

But, we will be told, this has as its precondition the *free* movement of precious metals on the world market and not only between countries producing them and those that do not, but also among the latter. Question: what about when there is a *violation of equilibrium* in the international distribution of metal, a termination of the free international movement of gold, as it was and is the case during and after the world war (also the United States formally banned export of gold from September 1917 to July 1919)? Does the law remain in force, that the value of gold in different countries is the same (that is, the difference is only a discrepancy in the costs for transportation)?

It has become a common place in the economic literature – it is asserted by Cassel and Hawtrey and *The Statist* [*a journal of practical finance and trade*] and others – that world *demand* for gold fell, due to the transition of most countries to paper inconvertible money, and together with this the *value* of gold decreased. This however is untrue. All warring countries sought to attract as much as possible to themselves more gold. The East (India, China), found itself in a pleasing economic situation, increased its demand for precious metals, whereas the supply – up to mid 1919 – was reduced. Gold is no longer functioning, as means of circulation, but its function as money *reserve* has increased to a much greater extent, and this is precisely due to violation of the former international *credit* relations, due to the disorder of the former complex and delicate *money–credit apparatus*. Despite all the obstacles, despite all the violations in international trade, gold, this universal commodity, still performed its international movement. The data, given by professor John Williams,[563] draw the following picture. During the war (1914–18) net import of gold in the United States was 1.04 billion dollars, most of which came from Europe. All the reserves of central banks of the main countries (excluding the United States) increased during this period from 2.24 to 4.07 billion dollar, and the increase was the result mainly of the recovery of gold *from circulation*. This recovery happened, of course, not because of a 'depreciation' of gold, but, on the contrary, because it maintained its value of money metal. From the armistice until May 1921, the import of gold in the United States amounted to 1.29 billion dollars, and export 724 million. Most of the outflow occurred between 1 November 1918 to 1 September 1920 'paying off adverse trade balances accumulated during the war with South American and Asiatic countries'. From 1 September 1920 to 1 May 1922 the import of gold in the United States was 1.05 billion and exports $109 million, that is the surplus was 941 million. And much of this gold flowed from Europe: from 1 November 1918 to 1 May 1922 the export of

[563]Williams 1922. Harvard University Committee on Economic Research.

gold from England and France to the United States amounted to 734 million dollars. But at the same time when a strong drain of gold toward the United States began in September 1920, the European countries in general have retained their gold reserves. The export of gold from Great Britain consisted chiefly of the South African output, while that of 'the Continent undoubtedly comes in large part from the Russian central gold reserve'. With regard to the change in gold reserves in Great Britain, in connection with the international movement of gold, we find in the *Manchester Guardian*:[564] 1) Most part of the major increase of gold reserves from November 1919 to March 1920 undoubtedly had its source in the strong inflow of gold from the Netherlands and Belgium in the previous five months. This gold flowed widely from Germany and was intended payment for America for food supplies. A whole part of it, 12.5 million pounds at least, entered at the disposal of the country. 2) Growth at the end of 1920 required, evidently, the inflow of gold from France, which had its source in Estonia. 3) Decrease of reserves in August and September 1922 is connected with the outflow of 3 million pounds to the United States ...' And, finally, the official data on outflow of gold from Germany in 1923. During the period from 28 February to 22 September there was forwarded for deposit abroad: to the National Bank in Bern 114.9 million gold marks and to the Bank of England 150 million. There was sold from 15 May to 7 September in New York 198.6 million, of which to meet the obligations of Belgium 60 million, and in London from deposits 38.7 million; a total of 237 million. In total was removed in less than six months 463.5 million gold marks.

These data show quite clearly that, despite the abnormal relations during and after war, gold continued to play its major role in international circulation as means of purchase and payment. Its function, as measure of value, as international means of exchange, as a national reserve, remained unshaken. And if there are no data for the assertion, that the value of gold has decreased due to reduction of world demand for it, then there are even less data for the assertion, that its value has decreased due to excessive production: from 1915 up to the 1922 world gold production decreased; from £96.4 to 64 million or by 33.5%; in 1923 it rose to £72 million. At the same time the *costs of production* grew together with the increase in commodity prices and the high cost of living ...

We can however be countered: does not the example of Sweden prove that the value of gold fell during the war? In the beginning the pound was above par in relation to the Swedish krona (19.43 against 18.06); from autumn 1915 it was below par, and it was possible to import gold. 'But – claims Cassel – the inflation sweeping the world dropped the value of

[564]See *Reconstruction in Europe* [series]. Special section of 16 August 1923.

gold so much, that it has become cheaper, than the overvalued Swedish currency'.[565] In order to prevent Swedish krona to fall in the wake of gold, Cassel says further, the law of 8 February banned free import of gold into Sweden. And this enabled the Swedish bank to obtain gold below the par of the krona...

The situation, however, was not so simple. We will now see, that the Swedish bank could cheaply buy gold due to *exceptional* reasons, which as little prove a fall of the *value* of gold on the world market, as the sale of our [Soviet] government, due to special conditions, in 1920/21 of gold abroad at a significant discount.

For Diehl it was not difficult to retort to Bendixen, who used the Swedish case for his nominalistic purposes as early as 1916, that Sweden, according to the accounts of persons informed in its operations, had the possibility to buy gold in *depreciated foreign currencies* and afterwards, get a *licence* for export [from the respective country] – 'that by means of buying a licence it was always possible' – to deliver it in Sweden, and the managers of the Swedish Bank, in the words of [G.H.] Kaemmerer, laughed about the version [story] of their fundamental rejection of gold...[566] But still it remains an open question also in Diehl: how it was possible to buy discounted gold also in depreciated foreign currencies? Let us return for the answer to Britain.

As is known, the British Empire accounts for a large part of world gold mining, and this share during the war grew in connection with the [greater] decline of world production than [that] in its Dominions, from 61.6% in 1915 to 66% in 1919. During the war Britain established control of gold throughout the whole Empire: it banned the sale of mined gold on the *free* market, and obliged to hand over gold at the old rate: 84 shilling 11 3/4 pence for a pure ounce without regard to the exchange rate, that is, to the *real* value of the *paper* pound. The lamentations of the gold producers did not receive satisfaction, since the appointed Commission concluded, that 'it is impossible to pay for gold more, than the value of money'. This corresponds precisely to the theories of Hawtrey, Bendixen and other nominalists, that it is not gold which determines the value of the pound, but the pound the value of gold! The whole incorrectness of this 'conclusion' of the commission became evident in 1919, when was allowed (and even then not entirely) the sale of mined gold (instead of the existing state reserves) in the open market, and gold miners proved, that they can sell more expensively [than what was] assigned. As a result, in December of the same year also on the London market the value of gold rose to 111s. 3d., that is, by 31% against [the one of] the 'Commission', and in February 1920 also to 127s. 4d., that is almost by 50%, while the

[565]Cassel 1922.
[566]Diehl 1918, p. 110.

premium on gold grew correspondingly with the fall of the paper pound.[567]

Thus due to the abolition of the free market, there was established a forced 'price' of gold, its value in Britain was lower than the actual one, and Sweden, taking advantage of its beneficial rate against the pound and 'buying licenses', could of course import to itself the 'discounted' gold.

Another example, of a somewhat different nature. The Indian government, banned the import of gold – and silver – on *private* account and taking advantage of the growth of the value of silver in relation to gold on the world market, the rupee to the sovereign and to the pound, bought in 1919 gold on the world market according to the American exchange rate to the pound and sold it on the domestic market *more dearly*...[568]

From the above data we draw the conclusions: In abnormal conditions the value of gold can be dissimilar in different countries; during the war, for example, due to the dearness of freight, of insurance, costs on the transport of gold had to grow, which must expand the boundaries of the gold points: up to 5% or more against 1 or even 0.5% normally. The value of gold may *artificially* fall, or rise against the real, world [gold], but this does not modify the position, that money is measured in the *world* value of gold: *real* money is always *world* money.

3.

We cannot here enter into a consideration of the question about precious metals, and especially gold, from all aspects. We will have occasion to dwell on it in connection with the analysis of the latest theory of money, credit, interest, conjuncture, and so on. Here we restrict ourselves to the most necessary. The analysis in the previous section showed us that the *value* of gold could not have fallen during and after the war. But Cassel and other latest theorists see the centre of gravitational motion of the exchange rate in the movement of commodity prices or, what is tautological, in the *purchasing power of money*, and that means also gold. Yes, the purchasing power of gold fell. This is an undoubted fact: in the United States, the country of gold currency, it fell in comparison with the pre-war period by one-third – according to the index of Irving Fisher. Does this not certainly prove the fall of

[567]For receiving sovereigns [the £1 coin, 0.233 ounce of pure gold] in London – before the war the world free gold market! – one must now present gold, which is bought on the market in paper, that is, in pounds at the rate of the day; in case of an exchange for a sovereign a pure ounce of gold is estimated in 84s 9d, which represents a premium on minted coin. Moreover for export of sovereigns a licence is required!

[568]See *Annual Financial and Commercial Review* of 1919 and 1920; *The Times* of 23 January 1920 and 28 January 1921.

the value of gold? Not at all. The movement of commodity prices is subordinate to its own laws irrespective of the movement of the value of a specific commodity, the money metal, which has a relatively high stability. It is not a discovery of today, that during the shifting phases of industrial cycles the relative value of money – gold – compared to commodities once falls in the phase of growth and prosperity, then goes up in the phase of crisis and depression. Fluctuations of commodity prices in these phases can happen both under a *constancy* of the value of money, and under a *change* of it... In his book (*The theory of social economy*) Cassel himself points out that periodic fluctuations of commodity prices, accompanying the so called (let us note: wrongly) *'small'* industrial cycles, *do not depend* on the movement of gold, but at the first occasion he forgets about this.

Thus, in the second *Memorandum* (in September 1921; the first in June 1920) the value of gold in Cassel unexpectedly grows: it 'is the most prominent feature of the monetary history of the past year'.[569] And this is explained by him above all by the strong flow of gold into the United States and, hence, the demand for it on the world market. Why did gold flow so much into America? Because, answers Cassel, there commodities could be bought cheaper, that is, gold was there more dearly...

First of all *the facts* speak completely different: for the period 1920–21 considered by Cassel, wholesale commodity prices in *gold* in the United States repeatedly crisscrossed with those prices in England (were once a bit higher, then a bit below); in comparison with the gold prices [commodity prices in gold] in France, Italy and Germany (that is, more inflationary prices) they were significantly *higher*. (Joseph Kitchin). Furthermore the *export* in 1921 from the United States was less than in 1920 by 1.8 times in value (364.9 against 673.4 million dollars on average per month). Finally, there was bought from the United States, despite the *unfavourable* exchange rate, because there was need *of food and raw materials*; the Americans reduced loans, American securities had long been sold out, paper currencies were accepted, of course, at an ever worse exchange rate, and it was necessary to pay with more gold. It should be recalled, that in 1920–21 a general *crisis* was raging on the world market with great force, and at such times gold is usually the most desirable means in *international* payments.

Yet Cassel does not limit himself to one explanation: he attempts to explain the rise of the value of gold also by a 'deliberate process of deflation' in the United States. Serious study, however, proved that deflation of *credit* in the United States happened only *after* the beginning of the fall of prices on the world market. But, observe, Cassel talks about deflation

[569]See Cassel 1921a, p. 124.

of *money*:

> Under ordinary circumstances, the endeavour of a country with a gold standard to bring down prices and thus to raise the internal value of its money would, according to classical doctrine, have caused an influx of gold into that country with a consequent increase in the total volume of the monetary purchasing power within the country. Thus, the depression of prices would have been counteracted and the internal value of the money of the country would have been brought down to that of gold. In the present case, this automatically regulating machinery has not had sufficient opportunity to work effectively. ... The gold which has gone to the States has not increased the circulation, or, more generally, the sum total of the monetary purchasing power within the country. On the contrary, this sum has been diminished. The deliberate deflation policy of the Federal Reserve Banks, has, by its severe restriction of credits, resulted in a greater monetary stock of gold now serving as foundation for a smaller volume of means of payment. Thus the depression of prices has continued and the *internal value* of the dollar has risen with the result that, instead of the dollar being levelled down to the value of gold, gold has been raised to the value of the dollar.[570]

Let us examine these arguments.

First of all this reference to the 'classical' currency–theory, which Cassel in his book himself acknowledges, is, at the least, deficient... Next is the remarkable explanation, that the automatic regulation could not appear in United States because, the flow 'has undoubtedly been made smaller than it would have been if the movements of gold had been quite free'. The strong, as we have seen, flow of gold, which went to the United States, in unprecedented fashion, and in addition still the cheap Russian gold, all this turned out insufficient for the implementation in practice in the United States of the 'classical' theory: this would have been, if it had been otherwise! But when and where was this 'classical' theory *automatically* fulfilled in practice?, we ask professor Cassel. It turns out that the gold flowing into the United States in 1920–21, contrary to the 'classical' theory, not only did not increase, as Cassel certifies, the quantity of money, but correspondingly diminished it! And, finally, the 'classical' conclusion of Cassel: the dollar banknote = coin = bullion lifted gold up to itself [the banknote], meaning, was higher than gold, which Cassel supports still thereby, that it

[570]Cassel 1921a, pp. 126–7.

was not the dollar [banknote] which has fallen to the value of gold! The whole error of these arguments of Cassel becomes apparent when one considers that, according to the 'classical' theory, gold – *bullion* – accumulating in 1921 in the United States in excess in relation to currency, should have fallen in value, and correspondingly the commodity prices risen in 1921. In fact there occurred just the opposite phenomenon. And how in Cassel does this fit in with on one side the claim, that gold on the *world* market rose strongly in 1921, and on the other – his statement that gold from all over the world came into the United States, where it was low in value, but artificially raised by the dollar [banknote]? And how could this dollar rise above gold due to deflation in 1920–21, when it was at this time *convertible*? However, all the contradictions of Cassel, related to his theory of money, are innumerable…

4.

When determining the exchange rate one should distinguish the question about parity and the question about deviations from it. Parity, as we pointed out, is determined by the value of money in relation to the commodity gold. If the currency of both countries – is gold (regardless of whether or not there circulates gold: gold–foreign-reserve system), then the parity is determined, as the *Bullion Report* defined it. If currencies are unstable, meaning not golden, let us call them paper, even if they were printed on silver, then the parity is still determined by the value for money of these countries, expressed in gold. If the franc due to inflation is regarded in gold as 1/4 of the normal, then the parity of the franc in relation to the golden dollar is 1/4 of the previous one, that is, instead of 5.18 francs to the dollar – 20.72. – Witte's [1897] reform, set the new gold ruble equal to the 2/3 the weight of the Imperial, that is, devalued it by 1/3, thus reduced its parity to the gold mark, gold pound or other gold money unit by 1/3 against the previous one. – And this is the case regardless of the *purchasing* power of the dollar in the United States, the franc in France – or the ruble in Russia, – that is, without regard to commodity indices, even if they were perfectly composed. *This is a fact*, no matter how it contradicts the philistine common sense, which appreciates money, by what one can buy with it, and not, how much it is of gold and no matter how it contradicts the commercial view, according to which the credit on one and the same sum of money has a different value in different places: in Cape Town or London (Hawtrey). This – is the law of developed commodity, capitalist, economy, which thus resolves the contradiction between use value, the usefulness of a commodity and its exchange value, between the

commodity and money, between commodity- and money capital.[571]

It is well known, that under stable – gold – currencies *fluctuations* around parity are common; in abnormal conditions the limits of the fluctuations, as we have already noted, expand. Under unstable paper currencies *deviation* from the old parity – is the norm. There is a change of parities, of equilibrium points, of fluctuation centres, and the fluctuations themselves acquire the strongest momentum. What is the cause of these *fluctuations*? – We now are not talking about change of parity. – Ricardo sought it in the varying quantity of money. He rejected the action of the balance of payments. He claimed – in a variety of his works – 'it rarely happens that the currency of one of other [country] is not redundant. It is

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[571]Keynes (1923), trudgingly following after Cassel, designs now a replacement of the automatic gold standard by managed money. But as it was correctly pointed out to him in the British banking press (*Westminster Bank review* [probably an article by Walter Leaf]):

Under an isometric money, whose purchasing power in relation to commodities would be held as constant as possible, except in relation to gold, the bill of exchange on London would cease to be world money for financing international trade. The bill of exchange in pound would no more be exchangeable for a determined weight of gold, measuring the value of the pound. Not a single country on a gold basis will be able to keep bills of exchange in pounds, as security for the money issued by it; and not a single foreign banker will longer wish to hold deposits in sterling, because the pound will generally purchase the same average number of goods, but not buy the same amount of gold, which is international legal tender.

This corresponds to a correct understanding of the essence of money and the exchange rate. We quote this from *The Times* of 31 December 1923, which does not prevent the same *Times* at another moment to consider, that the value of gold on the world market fell by 35%, evidently relying on the purchasing power of the dollar (20 February 1924).

Because of the importance of the question touched in the text, let us dwell further on the arguments of Reginald McKenna. In his report at the last annual shareholder meeting of the Midland Bank – 26 January 1924 – he among other things states:

It is often said, that money goes abroad or foreign money comes here (in England), but the fact is, that when gold is not used, money has no capacity for settlement. The title of money can change. Anybody can sell his sterling to the American for a dollar, but the American wants then sterling in England, and the Englishman the dollar in the United States. If there is a need to sell sterling, the exchange rate of the pound is lowered, and temporarily the British burden of payments to America grows. But the change of ownership does not move the money, that continuously remains and can be spent there where it was created. No foreign exchange transaction, no purchase or sale of property, no import of foreign goods or our export can take money out of the country or bring it here.

That which travellers take out – is insignificant... On this it is necessary to note to McKenna, that also under the existence of gold currency movement of gold is ever more reduced in comparison to the ever growing international settlement relations. Conversely, under the existence of paper currencies there took place also previously an international movement of it – for example, the Russian [paper] ruble before Witte's reforms into Germany. In recent years such a movement of money is observed *en masse et en grand*: for example, German marks into the United States, Sweden, Switzerland and others. In 1921, there was imported to the United States of foreign money (excluding silver and gold) for 100 million dollars. On the other hand, in countries with highly disturbed currency (Germany, Poland, and others) there is a large demand for dollars, pounds, guilders, not only as a means of accumulation, but also as a stable means of payment. A more or less stable foreign currency serves now as a means of ensuring the issuance of notes in several countries. Of Dutch guilders alone there are outside the Netherlands now 400 million... But usually the money is used in its place of issuance – Hawtrey too knows this; but that also facilitates gold, and thus also *real* money – and credit, – to be *world* money; everywhere real money can be exchanged for the same amount of money with different names, corresponding to the same weight of gold, that is, identical *value* and thus acquire a *purchasing power*, characteristic of the money of the given country at a given time. Another matter – also under normal circumstances – is the contradiction between money as a means of payment and savings, and money, as the measure of value, due to the variability of the value of money *in time* from the change of value of the commodity – gold; and, further, the change in *money* – gold – as means of purchase and payment, – *in time* in relation to the value of *commodities*. But this we will not dissect here.

redundancy or deficiency which is the *cause* of balances being paid from one to the other'.[572] This was wrong. But whereas Ricardo explained the *fluctuations* of the exchange rate, the *violation* of the equilibrium, with the quantity theory of money, the present innovators explain with this theory the (mobile) *equilibrium*, and the fluctuations – by the *balance of payments*...

To the extent that the Cunliffe Committee (on currency) in Britain or the Brussels Conference saw the main precondition of the establishment of stability of the exchange rates between individual countries in the stability of the money systems of these countries, they were right. And expressions of the kind, that 'the extraordinary American trade balance during the war has nothing to do with the weak currencies of Europe and nothing undertaken would be able to raise the exchange rate of Europe in New York, taking into consideration that balance',[573] miss the mark. This only proves, that under given external or internal conditions of the country, from whatever it had come about, a stable money system in them is *impossible*. True, during the war the United States through credit created a prop (pegging) of the exchange rate of their Allies without attention to their money system and money policy. But *à la long* this, of course, is impossible, also for the United States this was not a cheap cost. Without the prop, the exchange rates, as is known, did not hesitate to fly down. There is no doubt, that the stability of the exchange rate, a stable parity – whether the old or new – cannot be achieved for a long time, if the money system in the country is sick. But there is no doubt also, that under a regulation of the exchange rate – and in general the money system – of a given country one has to reckon also with international conditions (England!). If the assertion is one-sided, that 'the balance of indebtedness is controlled by the exchange rate',[574] equally one-sided is the statement of Cassel, that

> an adverse balance of trade, or even, more generally, an adverse balance of daily obligations is quite insufficient as an explanation of a lasting depression of the exchange value of the currency ... Now, if we are bound, on these grounds, to abandon altogether the popular theory of trade balances as an explanation of the movements of international exchanges since the beginning of the war, another very popular theory has to be buried too, viz., the theory that depressed exchanges can be corrected by adjustment of the trade balance.[575]

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[572]Ricardo 1895, p. 40.
[573]Falk 1922.
[574]Lindsay [probably paraphrase of 1898, pp. 50–1].
[575]Cassel 1921a, pp. 48–9.

The correct view is that the exchange rate depends both on the internal construction of the money system, and on the balance of payments of the country. This brings us close to the question about the balance of *payments*.

5.

The confusion, reigning in economic literature about the concepts of balance of trade and balance of payments [*platezhnyj*], flows not so much from the difficulty and complexity of the issue, but from the insertion in the same terms by different authors of different content. New terms or new adjectives to old terms, by which some authors try to dispel the fog, rather more concentrated it.[576] Essentially the present-day researchers in this area discovered nothing new. That, what Lansburgh objects to the vulgar economists in 1923 [article in Finn anthology] was formulated not worse, if not better, by Sartorius in 1907 and Soetbeer knew it very well in the 1880s [1875]. In general, economists, deserving that name, have more or less sorted out this matter. The situation is different with the views on the role of international trade- and payment relations in the movement of exchange rates: here the *dispute* and *errors* are for the most part *fundamental*.

For our task it is sufficient to firmly agree on the following:

Under the balance of *trade* understand only the *commodity* balance, the *visible* [balance] – without gold and silver; the excess of export of commodities of a given country above import or vice versa.

Under the [*current*] *account balance*[577] we will understand the balance of *assets and liabilities, credit and debit* relations of a given country to foreign countries, whether these relations are caused by a balance of trade, *invisible export* (in the form of transport, insurance, banking services, expenditure of foreign travellers and so on), export of capital in the form of precious metals or securities for commercial or other (war) purposes, payment of interest on debts or indemnity, in short, *in whatever form they are manifested and whatever caused them*.

The terms 'favourable' and 'unfavourable' balance we reject: they do not correspond very

[576]As example may serve the work of professor Boggs 1922.

[577][Finn-Enotaevsky uses the particular Russian phrase of *raschetnyj balans*, which for some Russian writers can mean the balance of payments (in its most common English definition), but this is not the case for Finn-Enotaevsky. We think he uses this Russian term rather for the concept of the 'current account' (or current account balance), hence we will translate it as such. In English the most common definition of balance of payments includes the 'current account (balance)' as part of it. The current account includes, but is broader than, the balance of trade. A 'balance' is a remainder, saldo, net amount, or difference after adding the two sides of an account.]

often with reality, they are remnants of the past (mercantilism). Let us agree on the terms: *positive trade* balance or positive current account balance, is understood, as the excess of export over import of commodities, respectively excess of assets above liabilities; *negative* trade balance or negative current account balance signifies excess of imports over exports of commodities – respectively liabilities above assets of the country. (The terms positive and negative are synonyms of the common terms: active and passive, but these latter applied to the trade- and payment balance are also *not* accurate).

Both the trade balance and the current account balance can be composed in different, but determined periods: at the end of each month, quarter of the year, a year or more. Whether they are positive or negative (active or passive), in the end these balances should equalise.

Finally, under the balance of payments of a country let us understand *payments of it or coming due to it at a given* moment.[578] The *difference* between payments of a given country and entitlements paid to it at a given moment, the saldo of mutual payments of two countries[579] at a given moment also determines the *activity or passivity* of the balance of payments of a given country.[580] The balance of payments is thus the trade balance *urgently* in a given moment, which is easily seen during a commercial–industrial crisis, when suddenly the sale of commodities is compressed and on the stage enters the requirement of payment in cash. The balance of payments is also the current account balance *urgently* in a

[578][This is a distinct conceptual definition of Finn, which Zvavich (1928) rejects.]

[579] [More accurate would be to say between one country and all others.]

[580]Let us illustrate what was said by a number of examples: According to data of professor Friday the excess of exports above imports of the United States to Europe for the period 1915–21 was 21.5 billion dollars, while the *trade* balance in relation to Europe was all these years positive. In contrast, imports of non-European nations into the United States exceeded exports to them for this period by 1.3 billion; in relation to the non-European countries the trade balance of the United States for all these years, excluding 1921, was negative.

According to the data of professor Williams (p. 619) the *current account* balance of the United States in 1921 was as follows: assets – 5176 million dollars, and liabilities – 5357 million dollars. That is, an excess of liabilities of 181 million dollars. The current account balance was thus passive for the United States. But it was not passive from the 'economic' point of view, but on the contrary, *active*: for 965 million dollars the United States provided *new* credits, yes for 32 million were purchased American securities, not touching other articles; and this, of course, went into the liabilities side of the balance...

The situation is different with *Argentina*: according to the current account balance, composed by Tornquist for two years from 1 October 1920 to 30 September 1922, the asset side was 1690 million gold pesos, and the liabilities – 1960 million; an excess of liabilities of 270 million gold pesos. And the '*economic*' result of this balance for the country according to Tornquist is liabilities of 374 million pesos.

Finally, England. An excess of import over export of commodities amounted in 1923 to £212,1 millions, that is, the balance of trade was negative. If we take into consideration the import and export of gold and silver, the excess of imports over exports amounts to £196,6 million. All 'invisible' exports for 1923 are £330 million. If we deduct from this amount the liability of the balance of trade (including also precious metals), interest on debt to America and other articles, which total £252 million, then the result shows an *active* balance of payments, a credit remainder, of £78 million. (article 'The Manchester Guardian commercial annual review', 31 January 1924 page 202).

There is no need to clarify, that, if the United States would have to pay its debit remainder for the whole of 1921 of 181 million dollars, let us say, on 31 December 1921 or England to receive its credit remainder for the whole of 1923 of £79 million on 31 December 1923, then this would have been a balance of *payments*, *passive*, for the United States on 31 December 1921, and a balance of payments, *active*, for England on 31 December 1923.

given moment. This can be seen *en grand* in the last days of the eve of the world war and its beginning, when all countries feverishly pulled together from international turnover [circulation] their funds. The balance of payments – active and passive – is the saldo of urgent payments of the country and to the country, subject to *immediate liquidation*, whatever the origin of these payments may have been.

Neither the trade balance, nor the current account balance *directly* affect the exchange rates. Whether a country is generally the debtor or the creditor in international relations, has no *direct* significance. What *directly* operates is *only* the balance of *payments*, *mutual payments of cash*, urgent in a given moment; *daily*, in the form of daily currency quotations. Along with the development of international trade and money–credit relations there developed technically also the apparatus to align the international payments. The number of credit agents reduced the need for moving gold also in international turnover to a minimum.[581] We will dwell here not on forward transactions, providing the user with the necessary means of payment without a counterparty risk, – that this is the soil also for speculation here does not interest us, – nor on arbitrage, giving the possibility of different means of international payment, scattered in different locations, to be concentrated at the site of most current demand, nor on credit operations, enabling deferred payments. For us it is important to emphasise the following: where and when arbitrage and credit is not sufficient for settling the payment, there and then appears on the scene, as reserve, gold. And if conditions of payment relations are such, that there is a long and a significant outflow of gold, which threatens the gold reserve of the country, concentrated generally in the national bank and employed still also for other purposes – domestic money circulation and the banking system, herewith we now do not care, whether the money system in the country is constructed on a proper basis and whether its credit policy is correct, – if, let us repeat, there takes place a drain of gold abroad, then a series of tested measures are adopted. First of all the lever of the discount rate is put into motion. This is immediately reflected on the interest of securities, circulating internationally and fluctuating in each country in price together with the fluctuations of interest rates. There take place also credit transactions of the given country with abroad and directly concern gold, due to the change of its interest rate, which

[581]As also old man Marshall pointed out in his latest work *Money, credit and commerce* (1923):
The international money market obtains ever more solidarity: the rates of discount, the prices of securities, and the prices of easily portable commodities vary in different countries less and less from their mean international level; and the exchanges are seldom allowed to move from par so far and so long as to cause any considerable futile movement of the precious metal: that is, a movement which is occasioned by a mere want of balance of immediate international claims, and would therefore be likely to need to be effaced by an opposite movement when these particular claims have been adjusted. ... (p. 253).
The matter with us is for now, of course, about normal conditions...

alters the flow of gold. But if this too does not suffice, which is common during commercial–industrial crises, then for the sake of the salvation of the gold reserves, and with this also the preservation of the monetary system, one does not stop also before the sale at *reduced* prices of commodities. Finally, in such times there takes place also such means of evening the payments, as *bankruptcy* of individual firms. We are not concerned with the question about the influence of interest rates on *commodity* prices; this is a complex issue, and we will analyse it in the article, dedicated to theories of conjuncture. Here we consider only the *relation* of the exchange rate to commodity prices.

The exchange rate stands in connection to the movement of gold, and the latter – with interest levels, but, as is known, the exchange rate may remain constant at varying interest levels, and the interest level may remain constant under a varying exchange rate. The outflow of gold, caused by an unfavourable exchange rate, *does not stand* in any *necessary* connection *with the movement of commodity prices*, contrary to the assertions of the theorists of the currency principle, and after them also by the latest innovators. *Facts* prove, that securities and commodities are exported then at *reduced* prices not because gold became more expensive in the country, due to its outflow, as also gold is exported at first not because it is *cheaper* in the country, – and this is also contrary to the remarks of Lansburgh (1923), – but because one does not want to or, more correctly, is afraid to sacrifice more gold, the basis of the whole money–credit system. For the sake of redemption of payments there is effected a sale also of commodities found already abroad at *reduced* prices. – One forgets in general the main feature of capitalist mass commodity production, which seeks foreign markets, guided herewith not only or even not so much by the high price, as by the volume of the market, as this was noted also by Hawtrey. Often the world market overflows with commodities also at *giveaway* prices, not being able to be realised, and this [is the case] especially during the periodic general crises. – There is no doubt, that when foreign exchanges [*devizy*: foreign currency reserves] worsen for a given country, then this is taken into consideration by exporters, engaging in trade transactions, whereby credits are created, who compensate for the increased demand for foreign exchange, all the more so as importers reduce transactions. But, firstly, herewith is proceeded from the already *existing* exchange rates;[582] secondly, this is *not at all connected with reduced* prices: also under unaltering

[582]Without going into an analysis of Hahn's theory – 'a synthesis of a theory of the balance of payments and a theory of inflation' – let us note, that his attempt to define the exchange rate based on the theory of marginal utility is at best a game with predetermined tasks and known results. As for the by him established *causal direct* connection between commodity prices and currency, we point out the following: It is well known, that every exporter and importer in their transactions proceeds from the condition of the currency and the condition of prices, but from already *given ones*. So, in Russia in the 80s and 90s of the last century, at the time of paper currency, each small exporter of grain knew well, that the exchange rate of the ruble he needs to search

prices the *export* abroad becomes – other conditions, of course, equal, – then advantageous, as also Cassel points out.

Let us repeat, only a strong outflow of gold, causing a number of measures in the *domain of credit*, may lead to a fall of commodity prices. But under normal conditions of the world market there can under unfavourable rates of exchange take place a *rise* of commodity prices – we are talking all the time about *exports*. So, 'in more distant countries, – Marx indicates, – where precious metal is not so easy to come by, if bills of exchange are scarce and insufficient for the remittances to be made to England, the natural effect is to drive up the prices of those products that are customarily shipped to England, since a greater demand for these now arises, with the purpose of sending them to England instead of bills of exchange; this is often the case in India'.[583] However, more recent observations show, that it may occur not only in remote countries but also in closer ones, like Austria-Hungary, under *paper* currency. Thus, in 1908 the expert Dr Bela Jankovich, showed in the bank inquiry Commission, that until 1892, that is before the establishment of the gold–foreign-reserve system in Austria-Hungary, the prices of *exported* commodities of the monarchy fluctuated to the same extent, as also the agio [premium] (on the foreign reserves) and in such a way, that prices of exported goods precisely then were particularly high, when the agio had increased... The reason for this that expert saw in the point that the monarchy, due to the lack of gold, could equate a passive balance of payments only by commodities... .[584]

'One pays, – says Cassel, – for foreign currency all the higher, the more that prices in foreign country B are low or the more that the level is high in country A, that is, the value of money is low here'. To say, that to pay for foreign currency [money] more, if one's own currency is depreciated, is precisely to say nothing. Question: need I pay for foreign currency more dearly, supposing that the domestic currency is *not* depreciated, when abroad one can buy for this foreign currency more commodities? Question: is the value of money in the country necessarily less, if prices have increased? And the question: does an increase [in the exchange rate] of foreign currency under an exchange for domestic currency show, that for this foreign currency can be bought more commodities in its [the foreign] country? *This* Cassel, or anyone else *has not proven*.[585]

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in the quotations of the *Berlin* Exchange – then the tone was set for us of the relation of the paper ruble against the gold mark – and about the price of wheat on the world market he needed to be guided by the quotations of it on the *New York* and *Chicago* Exchange: on the price of wheat in our ports was then decisive the influence of America. A *close* – needless to say– causal connection between exchange rates and prices!

[583]Marx 1981, p. 726.

[584]'Bericht der Bankkomission des Ungarischen Abgeordnetenhaus' (Budapest. 1908. p. 54.), quoted from Makai 1917. The theoretical views of the bank director Makai and Minister of education Jankovich with this do not interest us.

[585]It is characteristic, that the same economists, who put to the front the role of money as means of payment –

Cassel boils down everything to the movement of commodity prices. Should prices be constant – he says – then *occasional* fluctuations of exchange rates are evened out, [but] if prices rise, then exchange rates alter their parity. *Occasional* fluctuations of exchange rates happen besides the dependence on prices also due to the balance of payments.

No, let us object to this: prices can rise and fall, and the exchange rate will *not* alter its parity. So long as the *value* of money remains unaltered, the exchange rate will be stable and not alter the parity, regardless of the *increase* of prices. The exchange rate can fluctuate *occasionally* from the balance of *payments*, if the value of money is unaltered. A change of the balance of payments in dependence on prices, undoubtedly, can occur.[586]

How great the discord is among the present-day eminent economists in the question about the influence of prices on the exchange rate, is clear from the fact that for Cassel the condition for the stabilisation of exchange rates, the condition of the *fluctuation* of exchange rates around a stable parity, is the *constancy* of prices. Whereas in Lansburgh the stability of parity is achieved by *changes* of commodity prices! If you want – says Lansburgh – to regulate the balance of payments – under *paper* currency – you need to artificially induce the desire to export, and this by reducing prices. It is necessary for this to artificially raise the value of money by reducing the quantity of it. That is, it is necessary to artificially do that, what, in his opinion, is done automatically with gold currency. That is, it is necessary to apply the currency principle (on the basis of the exchange rate)... There is no need to show the bankruptcy of this theory, it was and is refuted also by life. In such a form even Lord Overstone, father of the Bank Act in 1844, could no longer defend it before the parliamentary committee in 1857.

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and see it [as] the *primary* function also in the history of the origin of money, whereas it is a more advanced form and was the basis of credit – that these same economists, proceeding in their analysis of money from credit, from credit money, highlight the role of money as means of circulation (currency), as means of *purchase*, when the question is about international payment relations. But, firstly, world money – gold in international relations plays the role not of currency, not a means of circulation, but a means of *exchange*; secondly, its role, as a means of payment with development of the global money economy, the global credit system, becomes *dominant*. No matter how erroneous the theory of money of Bendixen, he is nevertheless right when he says: 'the buyer acquires the bill of exchange not to buy foreign money, but to pay his debt and he does not care, how much or how little he buys for it. The relation of prices of his own and foreign countries does not interest him at all, but he is concerned only in particular about his commodity' (*Weltwirtschaftliche Archive* 1918). We quote this from the book by professor Schultze (1923). Of course, in abnormal conditions, under a regression in international relations, disorder of international credit, as this happened as a result of the war, the role of money as a means of purchase, increased. And Schultze is therefore right when he says: 'Nevertheless for the period of disorder the motto of Bendixen went too far, when he thought, that the "bill of exchange is dealt with not as means of purchase, but as a means of payment"' (p. 11).

[586]This is clearly illustrated by the following example. In view of the lowest value of Indian cotton in the world market, the contraction of world stocks of cotton and the uplift of the price for it, in the second half of 1923 demand for Indian cotton rose. This caused an export from India to Europe of the residues of the last crop and the conclusion of contracts for the new one. This improved the balance of payments and the rupee rose from September to November 1923 by 1 pence, that is, to 17 pence.

6.

As a rule, there is no *direct* connection between the exchange rate and commodity prices; there is an indirect connection, insofar as the value of money is altered, as also Diehl correctly pointed out. And not only, let us note once again, [there is] such an indirect connection, but [there is one] also through the influence of commodity prices on the trade balance, insofar as the latter through the instrumentality of *payments* affects the exchange rate. As a rule, let us repeat, exchange rates fluctuate around parity, based on the relation of the value of money of the compared countries in relation to the money metal – gold, and in no way around the purchasing power parity, which itself changes also under gold currencies, since commodity prices are changed by the conditions of production and exchange of commodities and besides that differences in different industries. That under *gold* currencies commodity prices do not alter the parity, neither Cassel nor Hawtrey nor other fans of the purchasing power of money can deny, although this stands in clear contrast with their theory, according to which the by them calculated purchasing power parity and the real gold parity would have had to coincide, which, however, is not so. This is even less so under paper currencies of two countries, which, for Cassel, represents 'the simplest case, giving the possibility to discover the real determination of the basis of the exchange rate', a basis, applicable also to the more complicated case of gold currency!..

For us, in contrast to Cassel, Hawtrey, Hahn, Bendixen, Heyn and many others, only the laws of gold circulation – are *normal*. Any *stable*, steady, money circulation is essentially *golden*; and it does not matter, whether in circulation there is gold, paper or silver. Every *unstable* currency is for us a synonym of paper – though it be silver; this – is an *abnormal, pathological* currency.

Pathology according to Virchow, is – 'physiology under abnormal circumstances'. Paper currency – is a disrupted metallic one; the laws of the first are – laws of the disrupted second. Hence the manifestation of rates of exchange under gold and paper currencies is *different*.

Under unstable, paper, currency the gold parity ceases to be a constant point around which the exchange rates fluctuate within certain limits. The exchange rate may deviate from it indefinitely. If there are temporary fluctuations around new equilibrium points, then these points are already new parities. In a country, where the standard is *silver*, the parity of the exchange rate alters in connection with the alteration of the value of silver to gold in the world market. It is enough to trace the movement of the exchange rate of the Shanghai tael in relation to the £ for 1920–23, to be convinced of this; fluctuations of it matched the silver

quotations on the London market in £; quotations of gold on this market correspond to the exchange rate of the pound to the dollar.[587]

Since under an unstable, paper, currency fluctuations of the value of money are due to the fact that the quantity of money *tokens* in circulation is higher or lower than the *required* level, defined by the *normal* – golden – currency and because this *latter* level *forcibly* is restored through increase or decrease of commodity prices, then it was and is falsely claimed, holding to the appearance, the surface, that *index prices* determine the value of money. And as, further, this same increase or decrease of the quantity of money tokens in circulation above or below the level, defined by normal – gold – currency, is forcibly restored in external money relations by way of a fall or rise of the exchange rate, then it is falsely claimed, that also these alterations of the exchange rate happen because of alterations of commodity prices or, what is the same, the purchasing power of money. In fact – we now are abstracting from the payment balance – both the alteration of exchange rates and of commodity prices are here the *consequence* of one and the same reason: alteration of the value of money. And this is not as a result of changes in the value of *gold*, but violations of the golden normal currency by the movement of money – *paper* – tokens.

It is entirely understandable, that, being under the influence of one the same cause, the movement of commodity prices and the exchange rate may show a certain parallelism, which will be all the more clearly expressed, the more in the change of commodity prices is manifested the change of the value of money-units, the monetary standard, as compared with changes of commodity values themselves due to changes in the conditions of production or market; and by this is explained the known parallelism between the movement of the real exchange rates and the movement of the calculated purchasing power parities. But about any correspondence of them there can be no question, on the contrary, very often these movements are different.[588] It is typical, that also under gold currencies the

[587]The attempt of India in 1920 to establish for the unstable, having become silver during the war, rupee a new parity in relation to the gold pound – in the ratio of 10: 1, instead of the former 15: 1 – and this in connection with an increase in the value of the rupee to the sovereign – suffered fiasco. The onset of a strong commercial-industrial crisis also in the East in 1920, a poor harvest in India, a reduction of exports, increased imports from Europe and a significant outflow of capital into England, 'earned' in India during the war and taking advantage of the favourable rupee exchange rate for relocation to the metropolis, – all this adversely affected the balance of payments. At the same time also silver on the world market has strongly fallen. The Indian government, having lost substantial amounts on the general sale of 'Reverse Councils' to support a stable exchange rate and on the sale of gold in order to reduce the premium on the sovereign, was forced soon to quit its venture. Fluctuations of the rupee in 1920 were: from 2s 9.5d to 1s 4.75d to the pound.

[588]Consideration of the 'index' question is not included in our present task. Note, nevertheless, that modern indices, even the best, are not suitable for comparing the purchasing power of money of different countries, and this is not only because of their different structure, but also different importance of the 'weight' of certain goods in the economy-wise different countries, the differences in prices of various goods and services in individual countries according to the degree of economic development, historical, cultural and natural environment. Also Fisher, who analysed in 1922 about one hundred and fifty existing indices, found the vast majority of them unfit

real exchange rate underwent seasonal fluctuations due to the movement of the balance of payments; this appears now also under paper currencies; the purchasing power parity 'is naturally less affected by them' – observes also Keynes.[589]

Since under *paper* – unstable – currency there are no boundaries to deviations from the constant gold parity, and if there are fluctuations, then [they are] around variable new points of equilibrium, then it is natural, that the effect of the balance of payments on the exchange rate increases. The trade balance and the current account balance in times of disturbed international relations and disorder of the money–credit apparatus pressurises more strongly on the balance of payments. The difference between them and the actual balance of payments diminishes – the urgency of their evening out is reduced – and one gets the impression, that they directly affect the exchange rate. And since as a result of the war the current account balance of European countries in relation to the United States became passive, then it is not surprising, that this is reflected in a prolonged reduction of their exchange rates against the dollar. It is clear, further, that political reasons, enhancing the disorder of international exchange and credit, strongly affect the fluctuations of the exchange rate of paper currencies (Ruhr!), which is reinforced further by the role of speculation, that precisely in such moments especially widely celebrates its orgies. Speculation uses not only existing disorder, but also emerging, grounded or not, fears for future deterioration (so in Britain in 1923 there was a response on pound sterling both from rumors about inflation, and the fear of a Labour government). In abnormal times the adjustment of short-term fluctuations, caused by the balance of payments, is accomplished with great difficulties. Credit in the country, not having a stable – golden – basis, loses to a large extent its force, as instrument of regulation of payments internally; the market of foreign exchanges [*deviznyj*] – the banks, the stock exchange – does not assume on itself the risk of varying exchange rates over time, and if assumes it, then with a great premium (Falk). Not having a solid centre of fluctuation, a constant determined golden centre of equilibrium, the fluctuations of exchange rates are subject to the pure laws of competition: there reigns contingency on the basis of everything changing in its value in relation to gold money...[590]

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as regards construction, and Sauerbeck's *Statist* index, with which by the way Cassel operates in his book, is enrolled among the group of 'worthless'. Keynes, Cassel, Marshall, Hawtrey, [Ernest Charles] Snow and many other authors bring a lot of criticisms about the current indices, but that does not stop the admirers of purchasing power to operate with them, attributing the non-correspondence of the calculated with the actual exchange rates not to the *unsuitability* of this instrument, for *this* purpose, but to the shortcomings of its construction!

[589]Keynes 1923, p. 101.

[590]How different can be the factors that influence the exchange rate, can be seen from the following examples: by itself *improvement* of the exchange rate may result in an outflow of capital abroad, placement of it in foreign companies and securities and thereby *worsen* the exchange rate. Increased taxation may cause capital flight from the country and thereby worsen the currency. There can be an increased demand for foreign currency due

7.

As we have already noted above, also under normal conditions of the world market with domination on it of a gold standard, commodity prices in different countries are different due to a number of economic reasons, wherewith agricultural products in backward countries, despite the low labour productivity, are lower in price, than in the developed capitalist ones (known examples are: England and Poland with Ricardo, England and Russia with Marx). Along with this there is manifested the tendency to the equation of prices in the world market. This tendency is enhanced with the development of international relations; also under constant exchange rates commodities naturally flock to where they are more expensive; this trend is manifested *in the parallelism* of price movements in different countries. However this process of price equation in the world economy finds a way to assert itself also in abnormal conditions. Analysis of commodity prices during the war in different countries, produced by Mitchell,[591] shows, that despite all obstacles, on a variety of conditions, in which are found the different parts of the world, a *uniformity* of price movements, although with tardiness in different countries, generally was manifested nevertheless *everywhere*. One should further compare the movement of prices after the war, bringing them to golden prices, to observe again in general the *parallelism* of their movement in different countries. And this is despite the obstacles, which came up against this trend of equation in the amplified 'currency chaos' after the war.

The exchange rate is a *symptom* [*indicator*] of the international payment relations of the given country, a symptom of the state of its currency. Talking about the exchange rate, as *about a factor*, acting on prices, is permissible only figuratively; this is only a shortened expression, but as a barometer does not make the weather, so also the exchange rate cannot 'regulate', cannot be also the 'cause' of international disturbances, as this very often can be read in present-day economic literature. But it *is led* in its actions by the industrial, commercial and credit world and it is from its side a symptom of results of accomplished actions in the world economy. Let us repeat once again: commodity prices in the world economy tend to equalise; commodities inside the country respond to the depreciation of money by an increase of their prices; world money reacts to depreciation of the national

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to a fall of the internal one, and this for hoarding purposes, which further deteriorates the exchange rate. Finally, there may be thrown into foreign markets large sums of money of the given country for the purpose of payment (reparations!) – which is connected also with internal inflation – and this especially worsens the exchange rate of the country...

[591]Mitchell 1919.

currency by its rise in relation to it; and this is reflected onto the exchange rate.

The characteristic feature of this money inflation – is an establishment of the strongest 'discrepancy' or 'divergence' [both terms in English in original] or, as it is not called there, a *difference* between *single* branches – and this especially over time. This is one of the characteristic features also of a '*Scheinkonjunktur*' or 'sham prosperity' [in English in original]. And this same inflation causes differences of *national* and *world* prices: a fall [?] of the former. But internal prices in the course of time align with world prices, and so there are required new factors, that are *independent* of prices, acting on foreign exchanges [*devizy*], in order to cause again this difference. This could be observed in Germany in recent years.[592] We will however not dwell on this phenomenon, we note, that the exchange rate does not reflect the internal purchasing power of money. Commodity prices *in gold* internally may be lower than the world commodity prices in gold. The *purchasing power* of gold internally may be higher than the world purchasing power of gold. Moreover, the *value* of gold internally may be higher than the world value of gold.[593] And nevertheless the rate of exchange *does not pay attention to this*, but only – to the relation of the *value of national* money *to world* money, to the value of gold *on the world* market. *Real* money – is *world* money!

That what was said by us corresponds with reality is evident:

1) From the movement of *commodity* prices under a stabilisation of the exchange rate. The exchange rate remains stable under a rise of commodity prices, seeking to equalise with world prices. Under regulation of stability the Austrian krone – since the time of the reform in late 1922 – proceeds from the exchange rate in relation to gold, and not [in relation] to commodity indices. Thus, the krone was quoted in New York on 7 December 1922 – 0.0014 cents, 6 December 1923 – 0.0014 and 7 February 1924 – 0.0014, meanwhile the Austrian index for this time rose: wholesale prices from 16.486 in January to 18.181 in December 1923... 'The most stable currency in 1923 in Europe, attracting foreign deposits into Riga'[594] – is the new Latvian currency, the Lat, based on gold, equal to a gold franc, and not [based] on purchasing power, that is, not on an index...

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[592]It is possible to recognise together with professor Bohn, that the strongest fluctuations of the rate of exchange in Germany got their impulse from the outside and [as] a result of political events. But small tremors proceeded also from inside – as we saw in 1922 – as a result of beginning inflation, which was used by currency speculators and commercial-industrial circles for an increase of the differences (that over time were being erased) between domestic and world prices. In this and in the other cases the *starting* point was not in prices, but in *currency*...

[593]Given the fact that also the *value* of a given national money on the world market, as it is expressed in the rate of exchange, can temporarily be different from the average value of it domestically, it is preferable [that] under a currency reform, under a fixing of the exchange rate, there is preliminarily [that is, in advance of the fix] achieved a prolonged stability of the exchange rate of money in relation to gold currency in the free internal market.

[594]*The Economist*, 16 February 1924.

2) If one takes the United States with gold currency and Britain with paper currency, then the exchange rate of Britain, as we already mentioned, alters in full compliance with the quotation of gold on the London market: a fall of the exchange rate on New York is expressed in a corresponding fall in the value of sterling in gold. But the exchange rate of sterling does not move in correspondence with the index of commodity prices in Britain or its purchasing power; there is no correspondence between the actual exchange rates and the 'parities' of the purchasing power...[595]

3) If we follow the course of the fall of the exchange rate in Germany in 1922–23 or in France in late 1923 and the beginning of 1924, then it appears, that the general depreciation began on the *world* market, that is, in the beginning fell the value of money in relation to world money, to gold on the world market; this gradually spread to the domestic market, causing a price uplift internally, and with it also inflation. That is, here there was a phenomenon similar to what takes place in normal conditions under a change of the value of gold on the world market, which is reflected in the beginning on foreign prices, that is, prices of commodities of foreign trade, and then proceeds with greater or lesser speed also on internal prices.

* * *

Our study leads thus to the following general conclusions:

1. Both under stable – gold – currency with constant parity, and under unstable – paper – currency with variable equilibrium centres (parities), the exchange rate or currency parity is determined by the ratio of the *value* of the money of the compared countries; the value of this money is determined by the value of gold *represented* by it, the value of this universal commodity on the *world* market. The exchange rate or currency *parity* is not dependent on commodity prices.

2. The shift of a given parity, that is, the point of equilibrium, the centre of fluctuations of exchange rates, to *a new one* occurs only from the change of the value of money – in relation to gold! – from whatever reasons this change might have happened.

3. Fluctuations in the exchange rate around a *constant* parity occur by virtue of the balance of *payments*, from whatever it was caused – the trade balance or the current account balance – and from whatever [position] it was changed, that is, becoming active or passive. In abnormal conditions the boundaries of fluctuations around *this* parity, that is the distance between the gold points, can move apart. Under an *unstable* currency with variable centres, the equilibrium of fluctuations occurs around these *variables* parities.

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[595][Table, see at the bottom.]

4. Under ever *falling* currencies these *deviations* – new parities and fluctuations around them – from the old constant parity can go to infinity (in Germany, for example, in 1923 from 7300 marks to a dollar to 4.2 trillion according to official quotations and 13 trillion on the 'black' market). If there is no constant determined centre of equilibrium, if there is a constant change of it, [then] competition is decisive: the law of supply and demand of foreign exchange [*deviz*], acting on the basis of permanent depreciation of the given national currency in relation to *world* money – gold.

[put this table in footnote 49:]

As an illustration, the following table:

1922 Average month	Wholesale prices on gold basis. Month. av. 1913=100	"	$ ex. rate on £ %	Wholesale prices in Britain in £	Parity of purchasing power £ to $ in %
	United States	Britain			
January	142	148	115.25	170	119.7
February	146	150	112	167	114.4
March	147	151	111	108	114.3
April	149	151	110	167	112.1
May	158	156	109.5	171	108.2
June	161	154	109.5	169	104.9
July	165	156	109.5	171	103.6
August	165	154	109	168	101.8
September	164	150	109.5	165	100.6
October	165	148	109.5	163	0.989
November	164	151	108.75	165	100.6
December	164	157	105.75	166	101.2

The first, second and fourth columns taken from the Federal Reserve Board, the third from *Manchester Guardian Weekly Commercial* 29 March 1923; *European Reconstruction* series. Section XIII. The fifth column computed by us according to the method of Cassel based on the first and fourth columns.

Chapter Twenty-Three

Review of Max Schippel, *The Currency Question and Social Democracy* (1896)

Karl Kautsky

Introduction by the editors

From the review by Kautsky of the German translation of Bastiat's *Maudit argent* [Damn money]:

> ... Money is, according to Bastiat, an instruction on services to be rendered and a payment for services rendered, which means nothing else than that the only commodity that is bought and sold is labour-power. This already sloppy claim is made even sloppier by the fact that Bastiat abstracts from the commodity character of both money and labour-power, the only thing the two have in common, and turns the money commodity into an instruction, and the commodity labour-power into a service. Unfortunately, neither Bastiat nor [the editor] Mr Dirichlet tell us how the miracle comes to pass, that two things having nothing in common with each other, such as a service and a coin, can be exchanged for each other. Surely only things of the same kind can be compared with each other, just as mathematical operations can be carried out only with magnitudes of the same kind. One can compare the labour time necessary for making a certain amount of money with the labour time required for the production of labour-power, but not a gold coin with an activity. But since Bastiat-Dirichlet do that, they also remain in the dark about the nature and functions of money, like the rest of theirs colleagues. *The damn money* indeed – a hard nut to crack for their wisdom teeth.[596]

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'Review of Max Schippel, *The currency question and Social Democracy*'

To date, the currency question has received comparatively little attention in our party. And that is quite understandable. For the wage-worker it has only secondary importance, and for the German wage earners its meaning was until now purely academic. Neither was any danger in the German Reich that bimetallism would replace the gold currency, nor was it to

[596]Kautsky 1886.

be feared that the workers of Germany would warm up for the cause of bimetallism.[597] The task of popularly presenting the currency question appeared, under these circumstances, not too pressing, and was made all the less attractive by the fact that is it a highly complicated question, extremely difficult to popularise.

But lately the currency issue has gained great importance. To be sure, the German workers in Germany are still completely cold vis-à-vis the silver men, quite unlike a part of the proletarians of the United States and some districts of England. But in the parties of economic reaction, and even beyond them, the supporters of bimetallism are experiencing rapid growth. The socially necessary production costs fall, the overcrowding of the markets is growing, prices fall, along with the rate of profit and, in many cases, the ground rent, and all the enterprises that do not or cannot adapt to these altered conditions are suffering. People do not want to admit that this is a necessary process that makes intolerable the capitalist mode of production for a growing part of the capitalist class itself, and are looking for the means to curb the calamity. Superficially, the whole trouble seems to be that the prices of commodities have fallen too much. To increase prices, to create an artificial rise in the cost of living – that has been for two decades already the tendency of the saviours of the hard-pressed sectors of industry and agriculture. This purpose should be served by the protective tariffs. The 'protection of national labour', launched with such great promises, has, however, proved its complete impotence; it has turned out to be completely unable to put a stop to the revolutionising work of the capitalist mode of production. The stronger that comes to light, the greater the number of those who cling to the new straw held out to them by the saviours of industry and agriculture: *devaluation* [*Geldverschlechterung*: depreciation of the currency].

The agitation for bimetallism has reached such height and extent, that it is necessary for our party to take a resolute stand on it. Schippel's brochure is thus most timely, and it has achieved the difficult task it set itself in admirable fashion. It exhibits all the strengths which we are accustomed to find in the works of Schippel: calm objectivity, simplicity, clarity of presentation and the use of rich material, selected and put together in a way that never overwhelms the reader or disrupts his train of thought, but animates it and makes it more insightful.

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[597][When the Reichsbank, under its president Dechend, stopped the sale of its silver, a 1881 article appeared by Heinrich Oldenburg, a Marxist who also wrote on value theory, that argued against this policy, which could undermine Germany's definite transition to gold currency: 'Toward clarification of the currency question'. In response to this, the young Schippel wrote an article (1882) arguing for the benefits of a low value currency system. In a letter to Engels (7 July 1882), Bernstein mentioned that Schippel's article was full of false arguments. Since then, Schippel had changed his position and now defended the gold currency (also see Schippel 1893, 1895).]

Only about one point we would like to make an observation. It does not concern things that the pamphlet contains, but some things that we do not find in it.

It is impossible to arrive at a full understanding of the currency question, without the necessary insight into the nature of money and its various functions as measure of value, means of circulation and means of payment, and the resulting manifestations of money as coin, paper money and credit money. Most errors on the currency question arise from the fact that people do not keep these functions properly apart.

Schippel has unfortunately refrained from discussing these functions of money. He jumps straight to the midst of things, and begins with the presentation of the victory of the gold currency. His presentation thus gains in vividness, because the reader is not tired by abstract arguments, but he must also fail to penetrate deeper into many questions.

We attribute to this circumstance, for instance, the fact that Schippel identified as the sole reason for the transition of modern states to the gold currency the cumbersome nature of silver, which makes it unsuitable as a means of circulation with the growth of trade. He says:

> With the higher development of capitalist production, which makes all economic relations dependent on buying and selling, which makes purchases and sales accumulate into ever more considerable sums, silver money itself becomes awkward in its clumsy masses, as it must be handed over and accepted in every nook and cranny of trade. Gold starts to be the *sole* basis of the modern monetary system (p. 3).

Why the *sole* basis? That is not explained by the reference to the needs of traffic. This merely explains why gold gradually pushes back silver, but not why it is the *only* currency metal. Precisely as means of circulation, silver remains in all countries massively in use as 'silver paper money'; that the difficulties of traffic of silver do not necessarily have to remove silver as a monetary metal is shown by East Asia, which draws its silver from Europe without any difficulty; and it was not difficulties of this kind, which led to the closure of the mints in India. Schippel himself says: 'The main Asian empires at any rate calculated in gold, and dealt with silver as a value *sign* for gold, even when their circulation consisted almost entirely of silver' (p. 38).

But this proves that the cumbersome nature of the silver as *means of circulation* was not the decisive reason for its dethronement. Much more important are the growing difficulties arising due to the use of silver as *measure of value* next to gold, and here also lies the weakest aspect of bimetallism.

Bimetallism requires not only that silver should be used in addition to gold as means of

circulation, but that silver should be legally brought into a fixed value ratio to gold, and that both precious metals should simultaneously be considered as measures of value [*Werthmaßstäbe*]. That was always irrational, and even in the past it often brought in its wake greater or lesser disturbances in the market, but it could still be employed to some extent at a time when the conditions of production and circulation in the main production sites of the precious metals, and therefore the values of these metals, changed only slowly and did not fluctuate too violently.

This has changed completely in recent decades. Trade in Europe and in the overseas countries has developed enormously. New production sites of precious metals are everywhere discovered and the technology of their extraction has been completely revolutionised. Therefore adhering to a certain value ratio [*Werthverhältniß*] between gold and silver has become impossible.

According to Soetbeer this value ratio varied from 1691 to 1830, from decade to decade, between 14.64: 1 (1771–80) and 15.80: 1 (1821–30). In the period 1831–73 the average annual value ratio amounted to a minimum of 15.19: 1 (in 1859) and to a maximum of 15.93: 1 (in the years 1833 and 1848) and 15.92: 1 (in the years 1845 and 1873).

How light are those fluctuations compared to those of recent years! The annual value ratio of silver to gold was, according to Lexis:

1887 . . . . 20.67 : 1	1891 . . . . 20.93 : 1
1888 . . . . 22.00 : 1	1892 . . . . 23.69 : 1
1889 . . . . 22.09 : 1	1898 . . . . 26.47 : 1
1890 . . . . 19.75 : 1	1894 . . . . 32.59 : 1

So in the last five years a minimum of 19.75: 1, and a maximum of 32.59: 1!

The bimetallists would have us believe, of course, that these fluctuations are solely attributable to the transition to the gold currency, and that they would disappear if the free coinage of silver were reintroduced. In truth, silver production would only add to these fluctuations. The following numbers can attest to the transformation in the conditions of production of silver: under the old value ratio annual silver production amounted to 140 million marks in 1841–50, to 158 million marks in 1851–55, to 161 million marks in 1856–60, and to 198 million marks in 1861–66. Thus they changed very little during that period. By contrast, we find in 1887 a production of 586 million, which increased rapidly until 1893 to 906 million.

Each of the two metals goes, or rather leaps, its own way, and it would be folly to want to

couple them together again. It would mean voluntarily introducing into our mode of production a new and powerful element of uncertainty, of fraud, of crises, and making the whole economic life even more dependent than before on the result of the fights and swindles of the cliques of high finance. The damage done to the working class by the fact that prices would rise, with wages following them only slowly, would indeed be the most immediate and, for the purposes of practical agitation, the most important consequence following from the introduction of bimetallism. But the enormous increase in general economic uncertainty would be the most important and the most destructive of its consequences, and it would hit not only the recipients of wages, salaries and interest, it would also hit those whose interests would supposedly be furthered by the dual currency, the small and even large entrepreneurs in industry and agriculture.

It is not their class interest, but the total lack of insight into the nature of money, which turns a part of the capitalists and landowners into bimetallists. And where this insight is lacking, also the workers can become admirers of the double standard [*Doppelwährung*: double currency], as the United States prove. Schippel rightly explains the bimetallic inclinations of many American workers partly from the fact that classes are not as stabilised in America as they are in Europe, and that wage workers still move strongly within the circle of ideas of the peasantry. To that should be added the special interest that the workers of the mine districts have on boosting silver mining. But yet another important element is added which Schippel does not mention, and which primarily acts on many of the best and most class-conscious workers who warmed up for bimetallism: the way in which, let us call it, *currency socialism* [*Währungssozialismus*], has evolved in the United States. This arises from the confusion in the concepts of money; on the one hand it is considered as a mere token of value, which does not need itself have any value, on the other hand money is equated with capital and the interest on capital is regarded as the *price* of money. The more money is available, the greater the competition of the owners of money among themselves, the lower the interest rate, the smaller capitalist exploitation, the easier the opportunity for non-capitalists to come into possession of the requisite means of production. The flooding of the country with worthless tokens of value is thus regarded as a safe means of breaking the monopoly of the capitalist class over the possession of means of production and of putting an end to capitalist exploitation.

This illusion has contributed not a little to get the vast majority of Anglo-American workers excited about paper money schemes in the 1860s and 1870s. Since then, the devaluation of silver has awakened the superstitious belief in the miraculous effects of debased money back

to life, in the form of the demand for the free coinage of silver.

Only through an explanation of the nature of money can these semi-socialist illusions be overcome. As difficult and dull as the theoretical discussions on this topic may seem, they have a great practical interest and without them one cannot reach complete clarity on the currency question. It would be a worthy addition to his excellent pamphlet if Schippel, on the occasion of a second edition, which hopefully will not fail to appear soon, were to insert a chapter on the nature of money.

Chapter Twenty-Four

From the New Literature on the Marxist Theory of Money[598] (1927)

Isaak Rubin

Herbert Block, *Die Marxsche Geldtheorie*. Jena, Fischer, 1926, 145pp.
Fritz Pollock, *Zur Geldtheorie von Karl Marx* (typewritten dissertation), 112pp.

Until recently there has been no specialised discussion in the economic literature concerning Marx's theory of money. While the Marxist theory of value has given birth to extensive critical literature, for the most part Marx's critics have silently avoided his theory of money or else have restricted themselves to cursory comments in passing. Certain contentious questions on the theory of money have been explored in the Marxist literature (particularly in the famous polemic involving Kautsky, Hilferding, Varga, Bauer and others), but we have almost no studies specifically devoted to a systematic exposition of Marx's theory of money as a whole.

The post-war period, with its phenomena of inflation and deflation, has provoked keen interest in questions of the theory of money and has spawned an enormous literature devoted to the problem of money and its circulation. This heightened interest in the problem of money cannot help but be reflected in literature devoted to the Marxist theory of money as well. More frequent references to his teaching on money are beginning to appear even in works that do not deal especially with Marx. In 1923 Feilen's capably written book – *Die Umlaufsgeschwindigkeit des Geldes* (1923, 142 pp.) – appeared and attracted considerable attention, declaring openly in the foreword that its constructions 'used' the foundations of the Marxist theory of money (although we should say in passing that it did so with considerable deviations and distortions).

Recently the two works mentioned above have appeared, being specifically devoted to exposition and analysis of Marx's theory of money. The work by Block came out in 1926, published by Fischer (in Jena); and Pollock's work, submitted in the form of a dissertation to Frankfurt University, remains unpublished. Both authors see fit to emphasise that their

[598]Translated by Richard B. Day, to whom we would like to express our gratitude. In *Die Marxsche Geldtheorie* (p. 98) Herbert Block (1903-1988) remarked on Marx's transformation table: 'Above all, however, Bortkiewicz overlooks the fact that the production price is not a monetary price, but like value is an expression for a certain quantity of labour time' (a point also made by Mandel 1984). Block became chief editor of the *Magazin der Wirtschaft* and in 1931 editor of the liberal *Vossische Zeitung*. He wrote the entry on money theories in *Handwörterbuch des Bankwesens* (1933). Block later emigrated to the U.S., where he was active at the Brookings Institution and the New School. In 1945 he became head of the Soviet Department of the Office of Strategic Services (the later CIA) and from 1950 he worked as chief economist of the Eastern Europe Division in the State Department.

theme is novel and has not previously been examined. Pollock says in his foreword: 'We have neither an exhaustive and systematic account (of Marx's theory of money – I.R.) from the author himself nor any thorough introduction written by an authoritative commentator.' Block says much the same thing: 'The literature has no such study devoted to Marx and the theory of money; this is very strange, for the Marxist theory of money follows directly from the Marxist theory of value, which has provoked such heated debates. My work aims to fill this gap.'

One has to say that these remarks by the two authors have some justification. There really are significant 'gaps' in the literature concerning the Marxist theory of money. This circumstance persuades us to pay special attention to the new works by Block and Pollock that aim to fill the gaps.

The presentation of the Marxist theory of money in the first section of Block's book (pp. 1–32) is, on the whole, completely correct and unobjectionable. Part of Block's contribution is that he does not restrict himself to presenting the role of money in a simple commodity economy but has also used chapters from Volume III of *Capital* that are devoted to an account of the role of money and credit in a capitalist economy.

The second and main part of Block's book (pp. 33–145) contains a detailed critique of the Marxist theory of money. The final two chapters, although included in the second section of the book, essentially have little connection with it and stand on their own: one is devoted to Marxist teachings on the role of money in a socialist economy, while the other is a brief account of Marx's 'philosophical' doctrine on money.

Block's critical argumentation indicates that he has studied Marx's work carefully and that the author has an ability to pose problems independently. Although the author mentions in passing that he is a supporter of the Austrian school (p. 44), he wants to give Marx his due. He acknowledges that even in the theory of money – which, in Block's opinion, is the least original part of the Marxist economic system – Marx showed himself to be 'a genius at synthesising' (p. 33). Among Marx's special contributions, Block includes his attempt to situate the theory of money within a general economic system and to present it as an integral part of the latter.

Yet Block's good intentions did not lead him to his goal or help him to penetrate, as we shall see below, the flow of Marx's ideas. This is to be explained, on the one hand, by Block's one-sided and mistaken notion of the Marxist theory of value, and on the other hand, by his somewhat formal-critical position, which discovers numerous contradictions in places where they either do not exist or can be easily surmounted.

Marx's doctrine on money is inextricably connected with his theory of commodity fetishism and the theory of value. Block knows perfectly well that Marx understands money to be 'a material precipitate of social production relations' (p. 134). But this '*social-philosophical*' definition of money, as he sees it, has nothing in common with a 'theoretical-economic' definition of money (p. 61). 'From the philosophical point of view, Marx understands money as a social relation that has been reified' (pp. 61–2). However, this philosophical definition of money bears no relation to economy theory, and thus Block considers it only in the final chapter of his book. As the subject of his immediate investigation Block takes Marx's purely economic teaching on money. 'By money in the economic sense, Marx understands a commodity that can assume, by virtue of its natural[599] properties, the function of universal equivalent in relation to all other commodities' (p. 62).

Severing the link between 'philosophical' and 'economic' teachings on money, Block commits an unjustifiable error. Both definitions of money are inseparably connected in Marx's doctrine. In fact, one cannot understand the Marxist teaching on the nature of money, as 'universal equivalent in relation to all other commodities', except on the basis of his doctrine of the reification of production relations between people. Block has torn Marx's teaching on commodity fetishism apart from his theory of money and thus foreclosed his way to a proper understanding of the latter.

If Block was completely unable to use the theory of commodity fetishism to understand Marx's teaching on money, the same must not be said concerning the theory of value. Block devotes considerable attention to the latter in both parts of his book. But Block understands the Marxist theory of value one-sidedly and mistakenly. This inevitably results in the misdirected character of his critical argumentation against the Marxist doctrine of money.

Block's one-sidedness lies in the fact that he studies the Marxist theory of money exclusively from the quantitative side and ignores the qualitative. The contradiction between private-concrete labour and social-abstract labour remains completely beyond Block's field of vision as he focuses exclusively on the contradiction between individual and social labour. In Block's eyes, the whole problem of value is reduced to the problem of socially necessary labour. Analysing the concept of socially necessary labour, Block hopes to find the key to all of Marx's supposed contradictions.

Block's one-sided depiction of the act of exchanging the commodity for money comes from

[599]Block is mistaken when he includes in the definition of money a reference to the 'natural' properties of the money commodity. Reference to the 'natural' properties of a given commodity (gold, for instance) can only explain to us why it is precisely this concrete commodity, and not some other, that emerges in the form of money; but it does not explain the emergence of nature of money in general. However, this error in Block's definition does not have any effect on the subsequent discussions.

his one-sided notion of the theory of value. For Marx, this act of exchange has two sides: the qualitative and the quantitative. First of all, it is because of the exchange of all commodities for one and the same money commodity that the values of all commodities appear as 'qualitatively identical' magnitudes, while the expenditures of private-concrete labour also appear as social-abstract labour. Money, therefore, figures as the 'reification of universal labour time' and as the 'social objectification of human labour'. In the second place, money also serves as measure of the magnitude of value on the part of commodities, which [value] in turn expresses the quantity of socially necessary labour expended on their production.

From what we have said, the reader will not be surprised to learn that the first – the qualitative – aspect of the act of exchanging the commodity for money has remained completely beyond Block's horizon. Money, as the materialisation of social-abstract labour, does not exist for him, so that he brings to the fore the role of money as an expression of the quantity of socially necessary labour. We might easily reconcile ourselves to such a one-sided presentation if Block more or less correctly understood the quantitative side of the act of exchanging the commodity for money. In Block's case, however, ignoring the qualitative side of this act is accompanied by a false description of the quantitative side.

Block suggests that money '*measures* the *socially necessary labour* contained in commodities and, by equalising it with its own substance of value, makes exchange possible' (p. 49. Our emphasis). While Block is convinced that his formulation accurately conveys Marx's meaning, this is far from true. Marx does not say that money 'measures' the quantity of socially necessary labour; money serves as measure of the magnitude of value of the commodities, which in turn expresses a quantity of socially necessary labour. If money directly measured the quantity of socially necessary labour, it would then be impossible to agree with Marx's famous comment that 'money does not directly represent labour-time itself'. The reader should not conclude that we are merely dealing here with a fortuitous error of formulation on Block's part. This formulation is connected, as we shall see below, with Block's entire conception. But let us provisionally set aside this mistaken formulation and consider essentially the act of exchanging the commodity for money.

In conditions of a simple commodity economy (and assuming that only a money-commodity functions as money, that is, some product whose production involves the expenditure of labour), exchange of the commodity for money tends to occur in such proportions that the quantity of socially necessary labour contained in the commodity equals the quantity of socially necessary labour contained in the money (that is, the money-commodity). Block takes this proposition, which results from the Marxist theory of value and money, as the

main object for his critical argumentation, although he never formulates and lays out his exposition directly but instead returns to one and the same question at various places in his book. In order that the reader might appraise Block's critical argumentation more readily, we shall arrange it in terms of the following three main questions:

1) Is equalisation of the labour contained in the commodity and the labour contained in the money the conscious goal of participants in exchange?

2) Just what is the socially necessary labour contained in the commodity?

3) Does it happen that the law of the equalisation of the labour contained in the commodity and in the money applies to each separate exchange transaction, or does this law have the character of a general tendency that is only realised when supply corresponds with demand?

In his responses to all of these questions, as we shall see, Block piles one mistake upon another, hopelessly confusing the exposition, and then he wants to hold Marx responsible for the confusion.

Consider the first question. Marx never claimed that the parties to exchange have the prior objective of complying with the law of equality of labour expenditures contained in the commodities being exchanged. Every commodity owner wants to receive for his commodity the greatest possible quantity of other commodities (or money) – and the unforeseen result of the intersecting wills and actions of a multitude of commodity owners, in conditions of a simple commodity economy, is the tendency towards an equality of socially necessary labour expenditures in the commodities being exchanged. But Block – who attributes to Marx the idea that money 'measures' socially necessary labour – comes to the absurd assumption that the owner of the money must know what quantity of socially necessary labour is contained in the commodity he is buying. 'We would have to make the fantastic assumption that the money – or, more accurately, the owner of the money – has a sixth sense that enables him rapidly to discern how much socially necessary labour is contained in the item he wants to buy' (p. 60). Block justifiably rejects such a fantastic assumption, but he completely misses the mark when he sees in it a logical conclusion resulting from Marx's teaching on money as the measure of value. Marx has no responsibility whatever for this fantastic assumption, which is contrived by Block himself.

Let us now turn to the second question. Beginning from his general viewpoint, which we have set out above, Block focuses his study and critical argumentation on analysis of the concept of socially necessary labour. In this regard, he finds in Marx a multitude of imaginary contradictions and ambiguities. We can summarise the pattern of Block's reasoning as follows.

Suppose that by socially necessary labour Marx understands 'technically average labour' (p. 49), which corresponds to the 'technological' or 'technically necessary value' of the commodity (p. 52).[600] In that case we have the following dilemma: either the commodity always sells at its value regardless of how much of it is produced, or else frequently – and even in most cases, when there is a lack of correspondence between supply and demand – the market price of the commodity is lower (or higher) than its value. The first assumption, although in Block's view it is more compatible with the Marxist theory of value and money, is clearly absurd. Marxists must therefore adopt the second assumption, which, in Block's opinion, essentially leads to repudiating the Marxist theory of value and money. First of all, it means that 'the value of the commodity depends upon the demand that exists for the given product. The result is to include subjectivist elements in an objectivist theory of value' (pp. 53–4). Secondly, given the assumption that prices deviate from value, 'unequal magnitudes of value are exchanged; for example, ten units of value in commodity form are exchanged for nine units of value in terms of money.…This conclusion contradicts both the Marxist laws of exchange and also the function of money' (p. 51). Third, and finally, the foregoing assumption leads us to the quantity theory of money, 'for the sum of money in the market depends not upon the sum of prices (commodities) it encounters; rather the sum of money at the disposal of demand, that is, the existing sum of money, is divided between the commodities whose prices represent some fraction of this sum of money' (p. 51).

The first of the three points that we have listed requires no special consideration. A lack of correspondence between the demand for commodities and their supply leads to deviation of their market prices from their value but, despite Block's opinion, does not alter the values of the commodities themselves.

As for the second point, of course every deviation of price from value means that the quantity of labour contained in the commodity, and the quantity of labour contained in the money (that is, in the money commodity), are not equal. But it never enters anyone's head to see in

[600]Block confuses his exposition by distinguishing 'technically necessary' value from 'socially necessary value', which he understands to mean a 'weighted average' of the individual values of all the separate exemplars of commodities of a given type (pp. 52, 95). For Marx, the concept of a 'weighted average' of labour and 'technically average' labour correspond: market value is always a 'weighted average' of individual values (which, however, we must not think of naively, in the way Block does, as the result of an arithmetic summation of individual values). Regardless of whether this 'weighted average' market value is defined as the value of labour with average productivity, or of labour with the highest or lowest productivity, it can be termed 'technical' in the sense that its magnitude is determined by the technical productivity of labour in the given branch of production, with its typically determined numerical relation between enterprises with different technical productivity. Confusing various instances of the determination of market value with instances of the deviation of market prices from market values, Block mistakenly thinks that in all cases when the 'weighted average' market value is determined by labour with the highest or lowest productivity this 'socially necessary' value deviates from the 'technical' value (p. 52).

this inequality, which accompanies the deviation of prices from value, a refutation of the Marxist teaching that a determinate sum of money, as the measure of value of the commodity, represents the stable axis around which market prices continuously fluctuate and with which they could only correspond in the theoretically conceivable condition of equilibrium between demand and supply. In fact, Marx himself pointed out more than once that 'This [exchange] relation [of the commodity for the money commodity] ... may express both the magnitude of value of the commodity and the greater or lesser quantity of money for which it can be sold under the given circumstances. The possibility, therefore, of a quantitative incongruity between price and magnitude of value, i.e. the possibility that the price may diverge from the magnitude of value, is inherent in the price-form itself'.[601] Distorting the whole sense of Marxist theory, Block suggests – and here we come to the third question posed above – that from Marx's point of view the law of value is precisely expressed in every single exchange relation. It is only by starting with such a false view that Block can come to the strange conclusion that 'Marx, unless he wants to reject his own theory of value and money, would have to presuppose that all commodities are sold according to average technical conditions' (p. 49) and in correspondence with their full value at every single moment.

Now we have to deal with the final point, to which Block attaches extraordinary importance and to which he returns throughout his book. It turns out that by recognising the possibility of a deviation of the commodity's market price from its value in cases when the equilibrium between supply and demand is disrupted, Marx capitulated to the quantity theory of money (pp. 51, 55, 112, and elsewhere). This objection is based upon a misunderstanding. In cases of disproportionality in production, for instance, partial overproduction of the given commodity, its market price necessarily falls below its value even if the quantity of money in the country perfectly corresponds to the requirements of the commodity turnover. One cannot even say that in this case the decline of the price of the commodity is the consequence of decreased demand as Block understands it, that is, the result of a diminished sum of money available to buyers for purchase of commodities of the given type. On the contrary, it often happens that if the price of a unit of the commodity falls by ¼, the general sum of such commodity units sold on the market increases even more, and thus the total sum of money spent by buyers to purchase the given commodity actually grows. In this case it is obvious that the fall in price for the commodity is in no way the result of a diminished sum of money, which therefore – despite the quantity theory – is not some magnitude given in advance and

[601]Marx 1976, p. 196.

cannot be taken as the starting point for the investigation.

We can see that recognising the possibility of the market prices of commodities deviating from their value does not in the least lead to recognition of the quantity theory of money. Marx's theory, according to which the quantity of circulating money corresponds to the needs of commodity circulation, does not prevent us from recognising the possibility of the partial overproduction or underproduction of commodities, with the accompanying deviations of market prices from value. But perhaps the teaching that we have cited from Marx, concerning the quantity of circulating money, excludes the possibility of general overproduction or crises? That is exactly Block's opinion: 'Marx's views, if consistently followed, must lead to denial of crises. For if the sum of money always corresponds to the sum of prices for the goods on offer, not a single product can remain unsold' (p. 103). The Marxist theory of money must lead us, in Block's view, to something that Marx himself ridiculed: 'the idea of economic harmony' (pp. 79, 81). This opinion on Block's part evidently follows from the naïve notion that the final cause of a change in the conjuncture is change in the quantity of money in circulation. But Marx, as we know, did not adhere to this naïve and superficial theory of crises. He viewed crises as the overproduction of capital and commodities, but he was by no means inclined to consider the cause of crises to be an inadequate sum of money in circulation.

We have to conclude that Block's basic critical argumentation is fundamentally incorrect. His effort to show that the Marxist theory of value and money leads to denial of the possibility of prices deviating from value is futile. Just as hopeless is his attempt to demonstrate that acknowledging the deviation of prices from value leads either to the impossibility of money fulfilling its function as measure of value or else to accepting the quantity theory of money (p. 55). If we do not understand the function of measure of value to mean – as Block does – some imaginary ability of money to measure directly the quantity of socially necessary labour in every commodity involved in every single exchange transaction, then money fulfils this function of measure of value even in those instances when the market price of the commodity is higher or lower than its value.

We have thought it necessary to give a detailed analysis of Block's short book because it represents the first attempt to offer, in systematic form, a critical analysis of the Marxist theory of money. We can deal more briefly with the short work by Pollock, since the author generally supports the Marxist theory and confines himself to an exposition of Marx's teaching on money.

Pollock's short dissertation (112 pages in length), which he submitted to Frankfurt

University, is devoted to a presentation of Marx's theory of money. The work consists of three parts. In the first part, the author clarifies the link between Marx's theory of money and his theory of value. The second and main part of the work is devoted to the functions of money. And finally, the third part briefly examines questions concerning 1) the quantity and value of money and 2) paper money, banknotes and (hard) currency.

As can be seen from this list of questions, the exposition is quite abbreviated and general in character. With short and succinct outlines, the author presents Marx's teaching on each of the points raised, occasionally supplementing it with his own explanations or critical scrutiny of the arguments from Marx's opponents. The author is a Marxist and, in general and on the whole, he conveys Marx's thinking quite correctly – not only when it is a question of presenting individual points of Marxist theory but also when it is necessary to elucidate the connection between these parts as well as their relation to the general foundations of the Marxist system.

The main shortcoming of this dissertation is, above all, its extraordinary brevity and summary exposition. The author moves quickly from one question to another without providing a more detailed analysis of each of them. In some places he expresses sound ideas, but without developing and substantiating them. For example, on a question that has provoked extensive debate – over which functions of money (as measure of value, means of circulation, and means of payment) are primary and which are secondary – Pollock (on p. 70) expresses the correct thought that for Marx all of these functions of money are secondary in relation to the primary function of money as universal equivalent. This idea requires explanation and justification, but we would look in vain for such justification from Pollock.

It is partly the brevity of exposition, and partly the author's refusal to provide a more independent and penetrating elaboration of his theme, that explains the strange fact that certain positions that play a central role in the Marxist theory of money are not considered at all by Pollock. As we know, Marx began his teaching on the nature of money with the contradiction between value and use-value on the one hand, and between private and social labour on the other. Pollock intentionally sets aside the first contradiction and justifies his strange indifference to the 'famous genesis of money from the contradictions of commodity circulation' by his reluctance to embark upon a broad investigation of the 'meaning of the Marxist dialectic' (p. viii). There is no need to demonstrate, however, that in a book devoted to Marx's theory of money there can be no justification for completely ignoring the aforementioned 'genesis of money'. As for the contradiction between private and social labour, Pollock – converging with Block on this point – one-sidedly regards it from the

quantitative side as a contradiction between individual and socially necessary labour (p. 12) without mentioning a word about the difference between concrete and abstract labour. Meanwhile, it is precisely the latter difference – not the former, as Pollock mistakenly thinks (p. 12) – that Marx had in view first and foremost in his doctrine of the 'dual character' of labour, which constitutes the necessary basis for the Marxist theory of money. Pollock correctly regards money as an expression of socially necessary labour, but he mentions not a single word concerning money as an expression of abstract labour.

Nor is Pollock's work free from certain mistaken and contradictory formulations. We note, for instance, that instead of speaking of the conversion of individual into socially necessary labour the author speaks of how individual labour 'is evaluated'[602] [*wird gewertet*] as some quantity of socially necessary labour – a formulation that Marxists cannot accept. On pages 98 and 99 the exclusive role of 'means of payment' is mistakenly attributed to a promissory note. On page 100 a promissory note, together with banknotes, is correctly recognised as 'the most important means of circulation for commodities'. Finally, on page 102 we learn that a promissory note is 'a means of circulation and payment'.

Summarising briefly, we can say that the works we have examined from Block and Pollock have not filled the gap in the literature on Marx's theory of money. Block's book is impaired by a biased viewpoint and a wealth of misunderstandings in the author's critical argumentation directed at Marx. On the other hand, we find in Pollock's book only an exposition of the Marxist theory of money without the slightest attempt at critical and penetrating analysis. It is extremely interesting that Block and Pollock, given the fundamental difference between their general points of view and their relations to Marx, converge on one point: they both consider Marx's theory of money on the basis of his doctrine concerning the contradiction between individual and socially necessary labour, while completely ignoring the contradiction between concrete and abstract labour. This indifference to the qualitative side of the problem of value foreclosed to both authors the path to a proper understanding of the Marxist theory of money.

[602][The word used in the text is 'ценится'.]

Chapter Twenty-Five

Against Idealist Distortion of Marx's Theory of Money (1930)

Bernard Berkovsky

We already referenced Berkovsky's *Essays on the Marxist theory of money* and his critique of Kautsky. He considered Kautsky to be a vulgariser and distorter of Marx's teaching on money. In *Economic doctrines* (1887) Kautsky starts correctly, recognising that value is a historical category, with an analysis of the development of the form of value beginning from the accidental form of value, as the contradiction inherent to the commodity, but goes off the rails when he explains the equivalent form as emerging from the practical difficulties of direct exchange encountered at a certain level. Berkovsky then cited a passage on quality and quantity from Marx's *A contribution*, also used in this article against Kushin. Berkovsky (1901–37) later headed a department in Gosbank. Ivan Kushin (1889–?), a prominent Menshevik leader (Secretary of the Moscow Bureau of the Central Region of the RSDLP), was numerous times arrested. Until 1923 he taught political economy at Moscow universities.

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Capital of Marx is an unsurpassed work, built on the application of the method of dialectical materialism in political economy. To systematically trace Marx's use of materialist dialectics over the three volumes of *Capital* and to express the results of such a study in a small book is undoubtedly necessary. Kushin's book *The dialectical structure of Capital of K. Marx (1929)* according to its author's statement also has as its goal to fulfil the specified task. However, the work of Kushin cannot be considered satisfactory, since it does not contribute to a proper mastering of *Capital*, on the contrary, in the reader it can create a false understanding of the foundations of Marx's political economy.

In the present article we do not intend to review the whole book of Kushin, we confine ourselves only to the critical consideration of Kushin's interpretation of Marx's theory of money. The character itself of Kushin's book and the purpose of our article predetermine the construction of the latter – the best way to detect the errors of Kushin is the direct comparison of the by him attributed views to Marx, with what Marx and his closest ally – Engels actually wrote.

As is known, the theory of money of Marx is the dialectical development of his theory of the

commodity, the theory of value. The discovery, made by Marx in the latter area consists of the detection of the dual character of labour, producing commodities – concrete labour and abstract labour. How is Marx's abstract labour represented in the light of Kushin?

> The labour of producers reveals, he says, its social character, only as indifferent, abstract, and, moreover, universal labour, because under this universal form of labour the commodity producers come near to an equally good labour in any field of social production. This – is in the abstract taken labour of all branches of production. This – is abstract universal labour ... A thing, acting as a commodity, should act therewith as a thing, deprived of *all its particular material properties*.[603]

Consequently, one of the characteristics of abstract labour is that it is a material labour, but at the same time deprived of *particular concrete properties*, for example, the property of the labour of a shoemaker, machinist, and so on. This interpretation of abstract labour is right and not contrary to the views of Marx. Nevertheless we were forced to stop at this point, because Kushin further on contributes to the concept of abstract labour a seemingly innocuous amendment, which in fact radically changes the notion of abstract labour, he omits the word 'particular' and treats abstract labour as labour, devoid of material properties in general.

On the same page we read further: 'Therefore, if a commodity must act as the embodiment of universal abstract indifferent labour, then it must act as a thing, consisting *as if not of a material, not of a substance*, but of one indifferent universal abstract labour'. On page twelve Kushin again treats value, and, consequently, its substance – abstract labour, as labour, devoid of *any* material properties. 'The product, being a particular use-value, is at the same also a value, a thing, devoid of *any material properties*'.

First of all, it is necessary to find out how Kushin on one and the same page gets along with such different treatments of abstract labour: the first abstract labour is labour devoid of specific material properties and the second abstract labour is labour devoid of all material properties, material properties in general. The issue, it seems to us, is explained by the fact that Kushin consciously or unconsciously goes on the beaten track of the majority of revisionists – in the beginning as a smokescreen to present a position close to Marx's, in order afterwards, when the alert reader is put to sleep, to start gradually carry through one's own views, different from Marx's.

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[603]Kushin 1929, p. 9. Everywhere my emphasis.

In the following we will be able to show that Kushin uses this technique repeatedly.
There is no doubt that Marx's abstract labour not at all is non-material. In support let us give excerpts from *A contribution* and *Capital*.

> Use values serve directly as means of subsistence. But, on the other hand, these means of subsistence are themselves the products of social activity, the result of expended human energy, *objectified labour*. As *objectification* [*Materiatur*] *of social labour*, all commodities are crystallisations of the same substance. The specific character of this substance, i.e. of labour which is embodied *in exchange value*, has now to be examined. ... *Labour which creates exchange value is thus abstract general labour*'.[604]
>
> By means of the value-relation, therefore, the natural form of commodity B becomes the value-form of commodity A, in other words the physical body of commodity B becomes a mirror for the value of commodity A. Commodity A, then, in entering into a relation with commodity B as *an object of value* [*Wertkörper*]*, as a materialization of human labour*, makes the use-value B into the material through which its own value is expressed.[605]

Kushin's treatment of abstract labour, in contrast to Marx's, is idealistic. Kushin's abstract labour is deprived not only of particular material properties, but also in general is non-material. Such type of abstraction is not at all in the spirit of Marx, Engels and Lenin, it contradicts the method of dialectical materialism. Non-material labour is a 'mathematical unreality', it is *only the thought* about labour. Such understanding comes very close to the interpretation of the latest bourgeois political economy, the so called social school.[606] Kushin's abstract labour is only a concept, expressing the social relation, divorced from the material process of production. This circumstance also gives us the right to say that we are in this case not dealing with dialectical materialism, but with idealism, because 'from the standpoint of dialectical materialism philosophical idealism is a one-sided, exaggerated, *überschwengliches* development (inflation, distension) of one of the features, aspects, facets of knowledge, into an absolute, *divorced from matter*, from nature, apotheosised'.[607]
The idealistic treatment of abstract labour by Kushin left its mark also on his understanding of money.

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[604]Marx 1987, pp. 270–1.
[605]Marx 1976, p. 144.
[606][Franz Petry, Alfred Amonn, Rudolf Stolzmann.]
[607]Lenin 1976, p. 361.

> Only money is the form of value, in reality, corresponding to its essence. Indeed in value should be expressed universal social labour in an abstract form indifferent for all of its particular manifestations. *Money expresses this labour not concretely*. *Money* does not possess itself all the particular properties of all particular products. *It expresses any type of labour only in the abstract* in a type of feature, common to all particular types of labour, if one distracts from all their particularities ... *Money serves as an abstract expression of universal social labour*.[608]

Since for Kushin abstract labour is not material, money cannot concretely express universal social labour, it serves only abstractly its expression. Kushin leads us, thus, into the mythical kingdom of shadows, devoid of everything material, concrete. The idealistic treatment of abstract labour brings Kushin in questions of money close to the nominalist theory, which, as is known, Marx believed to be profoundly erroneous.

> The fact that commodities are only nominally converted in the form of prices into gold and hence gold is only nominally transformed into money led to the doctrine of the ideal standard of money. 'Because tokens can be substituted for precious metals in the sphere of circulation, Berkeley concludes that these tokens in their *turn represent nothing, i.e. the abstract concept of value*.'[609]

Marx, who gave a brilliant critique of the nominalist theory of money, is represented by Kushin as an idealist-nominalist. Marx was not satisfied with criticism of various theories of money, including the nominalist, but contrasted them with his thoroughly materialist, dialectical theory of money. His conclusions on the discussed question boil down to the following positions: money is the universal equivalent. Social activity highlights from among the commodities one, particular commodity, and fuses with its natural form the universal equivalent. The money commodity – gold is the direct objectification, reification, the bearer of abstract labour.

> The particular commodity which thus represents the adequate *being* [*das adäquate Dasein*] of the exchange value of all commodities, that is to say, the exchange value of commodities regarded as a particular, exclusive commodity, constitutes money. It is a

[608]Kushin 1929, p. 19.
[609]Marx 1987, pp. 314 and 317.

> *crystallisation* of the exchange value of commodities and is formed in the exchange process. .. *Money is not a symbol*, just as the existence of a use value in the form of a commodity is no symbol.[610]
>
> The *body* of the commodity, which serves as the equivalent, always figures as the *embodiment of abstract human labour*, and is always the product of some specific useful and concrete labour.[611] Only a *material* whose every sample possesses the same uniform quality can be an adequate form of appearance of value, that is a *material embodiment of abstract* and therefore equal human *labour*.[612]

In the book of Kushin the views of Marx on the material being of money were reflected like in a curved mirror.

The commodity is a unity of use value and value, that is, a dialectical unity of opposites. This inner contradiction of the commodity is solved in its movement, the split into the actual commodity and equivalent and the transition of the commodity in the process of exchange in the form of the equivalent. How does Kushin depict this by Marx established resolution of the contradiction of the commodity?

> This contradiction, he says, is solved by the fact that the value of the commodity, for example, linen, is not expressed in its own, but in another use-value, for example, in a coat, possessing other material properties than linen and so representing the negation of all material properties of the linen (not only particular, but in general all material properties – B. B.). Then the linen as use-value and linen as value – are different things. Linen, if it acts as use-value, remains linen with its particular material properties. The same linen as value is a completely different thing, it is a coat. *Linen in this case ceases to be a contradictory thing*.[613]

Thus, the resolution of the contradiction of the commodity is equal for Kushin to its removal, destruction. To what extent does Kushin expound the actual point of view of Marx? Resort to the text of *Capital* shows that Kushin's resolution of the contradiction of the commodity stands in a screaming, not at all dialectical contradiction with the views of Marx. Marx felt it necessary to specially emphasise that the resolution of the contradiction consists not in its elimination.

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[610]Marx 1987, p. 289. [Berkovsky here lists further pages in *A contribution*.]
[611]Marx 1976, p. 150.
[612]Marx 1976, p. 184.
[613]Kushin 1929, p. 212.

> We saw, says Marx, that the exchange of commodities implies contradictory and mutually exclusive conditions. The further development of the commodity (i.e. of this process which reveals the dual nature of the commodity, being a use-value and value, and that leads to division of the commodity world into simple commodities and a money commodity) *does not abolish these contradictions, but rather provides the form within which they have room to move*.[614]

To remove, to eliminate the contradiction of the commodity only a socialist revolution is able. The socialist revolution eliminates the internal contradiction of commodity-capitalist society, that gives the product of labour the character of a commodity with the to it inherent contradiction between use-value and value. As long as there is a capitalist society, the commodity cannot, contrary to Kushin, cease to be a contradictory thing. Exchange spontaneously can only create the form, in which the contradiction *is manifested, realised and enabled*. This is the only dialectical method to solve the actual contradictions, so long as conditions are not ripe for the complete elimination of the conditions that give rise them.
That Marx thinks the resolution of internal contradictions in their external manifestation and realisation can be seen from the following:

> The *internal opposition* between use-value and value, hidden within the commodity, is therefore represented on the surface by an external opposition.[615] Both sides of this opposition are commodities, hence themselves unities of use-value and value. But this unity of differences *is expressed* at two opposite poles, and at each pole in an opposite way. This is the alternating relation between the two poles: the commodity is in reality a use-value; its existence as a value appears only ideally, in its price, through which it is related to the *real embodiment of its value*, the gold which confronts it as its opposite. Inversely, the *material of gold ranks only as the materialization of value*, as money. It is *in its reality* therefore exchange-value [*Es ist reell daher Tauschwert*]. (Additional evidence of Kushin's incorrect treatment of the expression of value by money – B.B.). Its use-value appears only ideally in the series of expressions of relative value within which it confronts all the other commodities as the totality of real embodiments of its utility. *These antagonistic forms of the commodities are the real*

[614]Marx 1976, p. 198.
[615]Marx 1976, p. 153.

> *forms of their motion in the process of exchange*.[616]

Whereas for Marx the resolution of the contradiction happens through the creation of forms for its realisation, the 'dialectic' of Kushin, stealthily, considers the resolution of the contradiction incompatible with its realisation. The 'dialectical' thinking of Kushin goes under the scheme of 'either–or' – either realisation, in which case there is no resolution, or resolution, in which case there is no realisation, but elimination, removal. But as far as we know, this kind of thinking is not called dialectical, but metaphysical.

The money-form of value, resolving the contradiction of the commodity, is the result of a lengthy historical, and, therefore, dialectical development. It is historically and logically preceded by the general form of value, which in its turn originated from the expanded form of value. The difference between the general form and the money-form is that the isolated position as a general equivalent became not yet the final destiny of one only specific particular commodity type. But under the general form too, unlike the expanded form, at any given moment the equivalent is one single commodity. The role of the equivalent is alternately performed by different commodities until, as a result of natural selection, the universal equivalent role transits to gold and finally is fused with it. The general [that is universal] form transits into the money-form. Kushin in the beginning gives a characterisation of the universal form of value, which coincides with that of Marx. He says:

> A coat, vodka, wheat, etc., taken singly possess now a form, expressing only their use-value. Their value has the form of linen, which is exchanged for them. *Their value possesses in this case only the form of linen and possesses no form of any other commodity*.[617]

Consequently, Kushin establishes, that under the general form only one commodity serves as equivalent. However, it is not this phrase which characterises the real views of Kushin, it is like in the definition of abstract labour only a smokescreen. The actual views Kushin appear after a few lines. Kushin continues:

> However, like the coat expresses its value by exchanging for linen, so linen expresses its value by exchanging for the coat. True, for the linen can be exchanged not only the coat, but also vodka and wheat, and iron etc. However, for vodka can be exchanged,

[616]Marx 1976, p. 199.
[617]Kushin 1929, p. 17.

> not only linen but also the coat, and wheat etc. So not only linen is a common form for the expression of the value of the coat, vodka, wheat, etc., but also the coat is no less the universal form for the value of linen, coat, wheat, etc. *Every commodity is the general form of value* of those commodities, that are exchanged for it, their general equivalent... *The general form of value ... again is converted into the expanded form of value.*[618]

Kushin does not see the qualitative distinction of the general form of value, in him it differs by nothing from the expanded form. Whereas Marx established that in this circle of commodity producers, connected by exchange relations, at any given moment only one commodity serves as universal equivalent, wherewith the role of this commodity alternately falls on the part of different commodities, Kushin believes that in the general form such an equivalent simultaneously are all commodities. Whereas Marx established that the general form transits directly into the money-form, Kushin states that general form again converts into the expanded form.

The following excerpt from *Capital* confirms the difference of Kushin's positions from Marx's.

> The universal equivalent form comes and goes with the momentary social contacts which call it into existence. It is *transiently* attached to this or that commodity in *alternation*. But with the development of exchange it fixes itself firmly and exclusively onto particular kinds of commodity, i.e. it crystallizes out into the money-form.[619]

In Kushin's statements about the general form of value was manifested a complete ignorance of the basic laws of dialectics.

According to Marx, as is known, the first form of value is the elementary or accidental [i.e. simple] form, the second form – the expanded form is the negation of the elementary form, the third form – the general form is the negation of the negation or a new affirmation. When in the role of universal equivalent definitively is asserted one single commodity the general form transits into the money-form. According to Kushin the dialectical development of the forms of value is different: the universal form of value once again converts into the expanded form, does not differ qualitatively from the first expanded form, from which the general form itself arose. Out of the second expanded form appears the money-form.

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[618]Kushin 1929, pp. 17, 18.
[619]Marx 1976, p. 183.

The 'dialectics' of Kushin is a vicious circle, in which is moving the category of one and the same quality, returning to its original position. A dialectics – very peculiar. In any case we did not find in Marx grounds for this kind of treatment of the dialectical development of the forms of value. It entirely is an invention of Kushin.
Turning to the individual functions of money, Kushin establishes the following distinction between exchange value and the standard of price.

> The transformation in the consciousness of commodity-owners of actual real commodities into ideal money is not an actual conversion of commodities into money. *Money is here only a qualitative material*, to which the commodities mentally are equated according to their quality. If the commodities are mentally deprived of their qualities and mentally transformed into gold, then after that by means of comparisons with a *determined amount of gold, taken for standard*, should *be determined what amount of gold* the given commodity represents in the minds of commodity owners. In this case, the value of the commodity will receive outward expression as the price of the commodity, that is, as a known *amount of gold pieces of a determined magnitude*. This form is the form of the price of the commodity. The price of the commodity is its value expressed in money. Insofar as money has only significance as a measure of value and standard of price, we are talking about money, existing only in the minds of commodity owners.[620]

The correct Marxist position, according to which in the measure of value one must distinguish two sides, in Kushin is turned into their division, the measure of value turns out to be only the qualitative measure, while the standard of prices is the quantitative measure of value. According to Marx the measure of value is both a qualitative and quantitative measure, and as to the standard of price, it is only a technical arrangement of the monetary commodity to perform the function of measure of value. In *A contribution* Marx wrote:

> Gold becomes the measure of value because the exchange value of all commodities is measured in gold ... The exchange value of all commodities is now expressed in gold. One has to distinguish a qualitative and a quantitative aspect in this expression. The exchange value of the commodity exists as the embodiment of equal uniform labour time, *the [magnitude of the] value of the commodity is thus fully expressed*, for to the extent that commodities are equated with gold they are equated with one another.

[620]Kushin 1929, p. 21.

> Their golden equivalent reflects the universal character of the labour time contained in them *on the one* hand, and its quantity *on the other* hand. The exchange value of commodities thus expressed in the form of universal equivalence and *simultaneously* as the degree of this equivalence in terms of a specific commodity, that is a single equation to which commodities are compared with a specific commodity, constitutes price.[621]

Thus, the establishment of both the qualitative and quantitative aspects of value relates to the function of measure of value, these are two sides of one and the same phenomenon inextricably linked with each other. Marx speaks about the exhaustive expression of the magnitude of the value of commodities [as] the function of the measure of value, speaks about the price of commodities long before he first utters the words 'standard of price'. The appearance of the latter he connects with a technical necessity.

> Given the process by which gold has been turned into the measure of value and exchange value into price, all commodities when expressed in their prices are merely imagined quantities of gold of various magnitudes. Since they are thus various quantities of the same thing, namely gold, they are similar, comparable and commensurable, and thus arises the *technical necessity* of relating them *to a definite quantity* of gold as a unit of measure. This unit of measure then develops into a scale of measure by being divided into aliquot parts.[622]

Marx repeatedly emphasised that the quantitative comparison must be preceded by a qualitative reduction to a unit.

> The magnitudes of different things only become comparable in quantitative terms when they have been reduced to the same unit. 'With reference to the magnitude of value labour counts only quantitatively, wherewith the latter *must be already reduced to human labour pure and simple*'.[623]

Nevertheless the distinction of qualitative and quantitative aspects of value and the establishment of their consistency in theoretical analysis Marx nowhere and never transferred into concrete reality. The commodity producer with his 'common sense' cannot

[621]Marx 1987, pp. 304–5.
[622]Marx 1987, pp. 308–9.
[623]Marx 1976, pp. 140–1, 136.

imagine the by him produced commodity as gold in general, to then imagine it like a determined amount of gold. As for Kushin, in him ordinary commodity producers, agents of commodity-capitalist society, are able to imagine the quality of value without quantity. In fact there is no quality without quantity, and no quantity without quality. Only in theoretical analysis can and should for a particular purpose (and only at a certain stage of the analysis) quality be considered separately from quantity, not forgetting that they constitute in reality a unity.

Money performs different functions, in particular it is treasure. Kushin sees in treasure the following contradiction:

> Firstly, all treasure one must regard as limited in its size by the amount of money. A limited amount of money can be turned only in a limited amount of particular commodities. Thus treasure is only a limited expression of the social character of commodity producers. *In it is expressed the particular private labour of a part of society, instead of the universal social labour*. True, treasure can be converted into a commodity of any particular kind. However, if in reality it will be converted into commodities of one kind, then it cannot be already converted into commodities of another kind. So, although treasure also expresses whatever type of labour, *it is always an expression of particular, not universal social labour*.[624]

Kushin is right when he looks for the contradiction of the function of treasure in the area of quality-quantity, but is wrong when, on the ground that this treasure can only be converted into a limited quantity of commodities, he declares that treasure is the expression of only particular, rather than universal social labour. Marx in contrast to Kushin, considers treasure only as a materialisation of abstract wealth of bourgeois society, that is, the embodiment of universal, abstract, social labour.

> Let us for a moment consider the commodity gold, that is money, in a state of rest and its relations with other commodities. … In contradistinction to commodities which only represent the independent form of exchange value, of universal social labour and of abstract wealth, *gold is the material being [Dasein] of abstract wealth. … Gold – is the material symbol of physical wealth* … As regards its form, it is the direct incarnation of universal labour, and as regards its content the quintessence of all

[624]Kushin 1929, p. 25.

> concrete labour. It is universal wealth in an individual form.[625]

The contradiction between the qualitative side of treasure, that is the fact that gold is the materialisation of universal abstract wealth and its quantitative limitation in individual commodity producers, Kushin 'resolves' in such a way that he entirely eliminates, reduces the qualitative characteristic of treasure. From the unity of opposites of quality–quantity, treausure is turned into a simple identity.

As with the resolution of the contradiction of the commodity by money, Kushin also in this case does not think of resolving the contradiction in any other way than by its removal. And this kind of dialectic is attributed to Marx, whereas he in the resolution of the contradiction of treasure gave a brilliant example of the application of the real dialectical method:

> The hoarding drive is boundless in its nature. Qualitatively or formally considered, money is independent of all limits, that is it is the universal representative of material wealth because it is directly convertible into any other commodity. But at the same time every actual sum of money is limited in amount, and therefore has only a limited efficacy as a means of purchase. This contradiction between the quantitative limitation and the qualitative lack of limitation of money drives the hoarder *again and again back to his Sisyphean task* of accumulation.[626]

Of what consists this Sisyphean work of accumulation, this endless process of formation of treasure? New formation of treasure is not conceivable without treasure not having to pass into its opposite, that is, without money not coming back into circulation. In order to multiply treasure the commodity producer begins anew the process of reproduction, money, found earlier in a resting situation flows into circulation as a means of purchase or payment for the instruments of production, raw materials, etc. With the development of the capitalist mode of production treasure in order for its multiplication can be, moreover, used by its owner in the quality of loan capital. Thus, the internal contradiction of treasure is manifested and resolved in the process of movement, in its transition into its opposite. It is characteristic for Marx that he considers the real dialectic to be in this case the rest as a moment of movement 'for it also remains in the circulation sphere as hoard, reserve, etc., even if only latently'.[627]

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[625]Marx 1987, p. 358.
[626]Marx 1976, pp. 230–1.
[627]Marx 1978, p. 213.

Continuing the analysis of treasure Kushin makes a new discovery.

> Insofar as treasure is taken out of circulation, the money, of which it consists, *is deprived of the ability to be turned* into other commodities. This is money which is deprived (for as long as it is treasure) of the ability to be a form for the expression for any labour, *except for the private, particular labour of gold manufacturers. It ceases to be the embodiment of social labour, that is, in general ceases to be money*.[628]

Here in Kushin everything is presented in a false way. Precisely because money is the materialisation of social wealth, because it possesses the quality of unlimited ability to transform into any commodities, it freezes into treasure. Precisely in the quality of real money, as opposed to the measure of value and means of circulation, it is a form of money, fused with the material form of a particular commodity, the material embodiment of universal social labour. The fact that the embodiment of universal, abstract social labour takes place in the form of the isolation of particular commodity – gold, is historically necessary for commodity-capitalist society owing to its intrinsic internal contradiction. The product of the private labour of gold industrialists enters into circulation as materialisation of universal social labour and remains in the quality of such, regardless of whether the gold is found in circulation or solidifies as treasure.

Money, says Engels in his review of *A contribution*, or simple circulation is then analysed in the second chapter, namely 1) money as a measure of value; 2) money as means of circulation and 3) *as the unity of the two aspects, as real money, which represents the entire bourgeois material wealth*.[629]

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So far we have discussed some positions, put forward by Kushin and shown, that they in no way reflect, what is really there in *Capital*. Now we can pass to more general questions. The first of these questions consists of the so called dialectic of concepts. The first chapter of Kushin's book is called 'Dialectics of the development of the commodity' and it is built on the principle of the self-development of concepts, without any connection with real processes, taking place in society. The second chapter argues, that the logical development of concepts does not match historical development. We for now leave the second statement and will focus only on the first. The question that interests us in this case is whether it is permissible to represent the dialectical structure of *Capital* as the self-development of concepts.

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[628]Kushin 1929, pp. 25, 26.
[629]Engels 1980, p. 477.

As an example of such a self-developing concept let us present the following excerpt from the book of Kushin: '*The concept of the universal form of value arises by itself from the development of the concept about the totally expanded form of value and is the negation of the latter*'.[630]

Marx in some places of *Capital* apparently gives occasion to such type of depiction of the dialectical structure of *Capital*, but precisely it is only in appearance. For example, speaking of the development of the forms of value, Marx, by the way, says: 'the simple form of value automatically passes over into a more complete form'.[631] However, comparison of these extracts from Kushin and Marx shows, that they are speaking about different things: in Kushin a *concept* about form arises *by itself* out of the development of the *concept* about a different form, in Marx the *form as such* arises by itself over another form; in Kushin the emergence of the concept is the result of the logical exercise of the thinking subject, in Marx the development of *forms of value – is an objective process*, and the development of concepts only the reflection of that process. On the same page 154 Marx explains how the elementary form itself transits into a more complete form.

> Therefore different simple expressions of the value of one and the same commodity arise according to whether that commodity enters into a value-relation with this second commodity or another kind of commodity. ... The isolated expression of A's value is thus transformed into the indefinitely expandable series of different simple expressions of that value.

Kushin employs the *form* of the first chapter of *Capital* in order to portray Marx with the purest water of the Hegelianists, but if Kushin were an objective researcher, he would have revealed behind the form of the first section of *Capital*, in which, as Marx himself says, he coquetted with Hegelianism, its real materialist content. Kushin is guided, evidently, by the preconceived goal – to present Marx not as a materialist, but an idealist, therefore he in every possible way emphasises the form of *Capital* and therewith undoubtedly distorts it.

To depict the dialectic of *Capital* as the self-development of the concept, after what has been said by Marx and Engels on Hegel's method is simply monstrous. Engels, for example, wrote:

> According to Hegel, dialectics is the self-development of the concept. .. It develops into itself through all the preliminary stages which are all included in it. .. This

[630]Kushin 1929, p. 15.
[631]Marx 1976, p. 154.

> ideological perversion had to be done away with. We again took a materialistic view of the thoughts in our heads, regarding them as images of real things instead of regarding real things as images of this or that stage of the absolute concept.[632]

Marx, who in the afterword to the second edition of *Capital* formulated the difference of his dialectical method from Hegel's method,[633] in fact, still in *A contribution* negatively commented about the logical self-development of the concept, which Kushin attributes to him.

> To philosophical consciousness —which regards the comprehending mind as the real man, and only the comprehended world as such as the real world— concrete totality, regarded as a conceptual totality, as a mental *concretum*, is in fact a product of comprehension; yet *it is by no means a product of the self-evolving concept whose thinking proceeds outside and above perception and conception*, but of the assimilation and transformation of perceptions and images into concepts.[634]

We could double or triple the excerpts from the works of Marx and Engels, however, we think that the given is enough to confirm our thought, that to portray the dialectical structure of *Capital* as the self-development of the concept, is to mock this outstanding monument of materialist dialectics.

The second general–theoretical position put forward by Kushin, is that the logical development of concepts does not coincide with the historical development. With this Kushin seeks to complete his idealistic depiction of the dialectics of *Capital*. The general formulation of this thesis is given by Kushin in the following mode:

> The development of the concept about the commodity already conceals in itself the development of the concept about a society of commodity producers ... here it should be noted on the one hand, that the transition from the most simple undeveloped form of the concept about society of commodity producers towards the developed concept about real particular forms of that society does not at all coincide in general with the development of the same society of commodity producers in historical reality out of its most simple and undeveloped forms until the transition of capitalist society into communist society. On the other hand, the circumstance should not be forgotten that

[632]Engels 1990, p. 383.
[633]See Marx 1976, p. 102.
[634]Marx 1986a, p. 38.

> to a certain extent and in certain degree such coincidence exists.

The latter 'on the other hand', that is the recognition by Kushin of a correspondence of logical and historical development is, as one would expect, only a fig leaf. When Kushin goes to particular forms of value and associates them with historical processes of development of commodity society, he 'specifies' this thought – coincidence is only in appearance, only on the surface and to a limited extent, in essence there is none. Thus, remains valid only the thought expressed in the phrase by Kushin, starting with the words 'on the one hand', that is, that the logical development of the concepts does not coincide with the historical development of commodity society. Like also in the whole book this position too is attributed by Kushin to Marx.

The actual views of Marx and Engels have nothing in common, however, with this kind of positions. Talking about the revolution, produced by Marx in dialectics, Engels concludes: 'Thereby the dialectic of concepts itself became merely the conscious reflection of the dialectical motion of the real world'.[635] In *Dialectics of nature* Engels also wrote that the dialectical laws are the laws of real development.

> We are not concerned here with writing a handbook of dialectics, but only with showing that the dialectical laws are really laws of development of nature, and therefore are valid also for theoretical natural science. 'We consider it necessary to emphasise here that the primacy for judging the correctness of the dialectical laws is their effectuation in the real development of nature, only in this they are valid for the theory of science'.[636]

In direct relation to our subject matter Engels expressed his view in a review of *A contribution* in the following words:

> *The logical method of approach was therefore the only suitable one. This, however, is indeed nothing but the historical method,* only stripped of the historical form and diverting chance occurrences. *The point where this history begins must also be the starting point of the train of thought*, and its further progress will be simply the *reflection*, in abstract and theoretically consistent form, of the historical course.[637]

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[635]Engels 1990, p. 383.
[636]Engels 1987b, p. 357. [The second sentence we do not find exactly in Engels. Perhaps it is Berkovsky's own.]
[637]Engels 1980, p. 475.

Indeed, the cited authoritative judgment of Engels is entirely enough to reject in general Kushin's statement that the logical development does not correspond to historical development, but it is not out of place to show that the concretisation of this thesis as applied to the development of the form of value reveals the polar opposite between the presentation of the ideas of *Capital* by Kushin and its actual content.

The first form of exchange value is the elementary or accidental form.

> In historical reality, says Kushin, contact of independent of each other communities led towards the appearance between them of trade, which originally took place only by chance in a few cases. This elementary trade in its apparent [*vneshnej*: outward] form is the realisation of the concept about the elementary accidental form of value. However, if, on the one hand, apparently [in outward form] this exchange also possesses the simple form of value, then, on the other hand, as such, it possesses not yet this form.[638]

So, for Kushin the elementary form of value essentially in practice never was realised in history. According to Marx, on the contrary, it is found in practice precisely at the first stages of development of commodity society. Analysing the elementary form of value, Marx concludes: 'It therefore follows that the simple form of value of the commodity is at the same time the simple form of value of the product of labour, and also that *the development of the commodity-form coincides with the development of the value-form*'.[639] This extremely important methodological remark of Marx predetermines the solution of the question as a whole – the development of the forms of value coincides with the development of commodity society. In the following it is necessary only to illustrate the coincidence of individual forms with determined stages. In particular, a few pages later, Marx returns to the simple form of value, and says 'this form, it is plain, appears in practice only in the early stages, when the products of labour are converted into commodities by accidental occasional exchanges'.[640] Whereas Kushin states that the simple form essentially does not exist, Marx indicates that this form occurs in concrete reality with the emergence of commodity society. Unlike Kushin, Marx makes not any clause that it is found just apparently [outwardly], and not essentially.

The second form of value – is the expanded form. Concerning this form Kushin says

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[638]Kushin 1929, p. 25.
[639]Marx 1976, p. 154.
[640]Marx 1976, p. 158.

> Development of a society of commodity producers in historical reality again reveals features of similarity with the development of the concept about this society. The contact between the separate communities, taking place in the beginning in accidental or elementary cases of exchange, entails an extension of this exchange contact and repetition of cases of exchange. Products of one community begin to be exchanged for a variety of products of other communities. The decomposition of primitive society thereby gets a new particular form, which is the negation of its particular forms, when exchange carried the character only of elementary accidental events. Exchange now acquires in its apparent being [outward form] the realisation of the fully expanded form. However, also in this case exchange at the heart of the matter lacks that form.

As one might expect, the real point of view of Marx on the existence of this form in practice is the direct opposite of the assertions of Kushin. 'The expanded form of value comes into actual existence for the first time when a particular product of labour, such as cattle, is no longer exceptionally, but habitually, exchanged for various other commodities'.[641] Also in this case Marx makes not any clause about only the apparent realisation of this form, but simply says that this form is realised, therefore, not only in appearance, but also according to its content.

The third form of value – is the general form. Also in this case Kushin posits only a superficial coincidence with the real development of the society of commodity producers, however, 'a real coincidence between the development of the concept and the development of reality itself there is here not'.[642] The reason, according to which there is no real coincidence, Kushin sees in the point that 'production for own consumption maintains dominant importance not only at the time when there arise just the first germs of commodity exchange, but also when the individual products already are produced directly, as commodities, having the significance of universal equivalents'.[643] Consequently for Kushin also under the realisation (only apparent, it is understood) of the general form of value production for own consumption remains dominant. We read something different in Marx. '*This division of the product of labour into a useful thing and a thing possessing value appears in practice only when exchange has already acquired a sufficient extension and importance to allow useful*

[641]Marx 1976, p. 158.
[642]Kushin 1929, p. 100.
[643]Ibid.

things to be produced for the purpose of being exchanged, so that their character as values has already to be taken into consideration during production'.[644] Let us note that, firstly – the general form of value for Marx is realised in practice, and, secondly, only then, when determined material conditions are ripe, when exchange has already acquired sufficient extension and sufficient importance, and this of course cannot take place, if production for own consumption remains dominant. The last form of value – is the money-form. Its emergence too [according to Kushin] does not correspond to the development of commodity society. The reason for the mismatch, Kushin sees in the fact that

> a sufficient condition for the separation of money from the rest of the commodities in historical reality is the transformation of surplusage from a random into a more or less permanent phenomenon... This society as a whole remains a society in which production goes into consumption without the mediation of exchange. The development of a thin layer of commodity society, although [it] also attained already the money-form, nevertheless is still determined by the development of the dominant social form of production for own consumption, not transforming society as a whole in a society of commodity producers.[645]

We have just shown, that it is not true that for the isolation of a universal equivalent the transformation of the exchange of the surplusage from an accidental into a permanent phenomenon would be sufficient. Such transformation is sufficient only for the dialectical transition from the simple form to the expanded form. For the emergence of the general and its subsequent money-form it is necessary that production has as its predominant purpose exchange. Only 'the gradual extension of barter, the growing number of exchange transactions, and the increasing variety of commodities bartered lead, therefore, to the further development of the commodity as exchange value, stimulate the formation of money and consequently have a disintegrating effect on direct barter'.[646]

Now, we turn attention to the statement of Kushin that the emergence of the money-form is localised [in] a thin layer and has no effect on society as a whole. Yet Marx and Engels emphasised the revolutionising influence of money on all of society.

> Once, says Engels, the commodity-producing society has further developed the value

[644]Marx 1976, p. 166.
[645]Kushin 1929, p. 107.
[646]Marx 1987, p. 291.

> form, which is inherent in commodities as such, to the money form, various germs still hidden in value break through to the light of day. The first and most essential effect is the generalisation of the commodity form. Money forces the commodity form even on the objects which have hitherto been produced directly for self-consumption; it drags them into exchange. Thereby the commodity form and money penetrate the internal husbandry of the communities directly associated for production; they break one tie of communion after another, and dissolve the community into a mass of private producers.[647]

Also Marx speaks about the same:

> The exchange of commodities begins where communities have their boundaries, at their points of contact with other communities, or with members of the latter. However, as soon as products have become commodities in the external relations of a community, they also, by reaction, become commodities in the internal life of the community.[648]

So, we come to the conclusion that the development of the form of value corresponds to the development of commodity society, the development of the original undeveloped contradiction of the commodity, hidden, dormant in the product, becoming a commodity. The process of the development of production from production for self-consumption into production of commodities coincides with the development of the forms of value. On this eloquently testifies the following excerpt from *Capital*:

> The *historical process* of the broadening and deepening of the phenomenon of exchange develops the opposition between use-value and value which is latent in the nature of the commodity. The need to give an external expression to this opposition for the purposes of commercial intercourse produces the drive towards an independent form of value, which finds neither rest nor peace until an independent form has been achieved by the differentiation of commodities into commodities and money. *At the same rate, then, as the transformation of the products of labour into commodities is accomplished, one particular commodity is transformed into money*.[649]

[647]Engels 1987a, p. 296
[648]Marx 1976, p. 182.
[649]Marx 1976, p. 181.

In the proof of a mismatch of the logical development of the forms of value with the historical development of commodity society Kushin used one and the same method, he showed that this form supposedly superficially is realised in practice, when all the material preconditions were not ripe for its actual realisation. But to prove this entirely unprovable position Kushin chooses the following method. He portrays the case as if all forms of value are concepts about fully developed commodity society. So, the simple form of value

> is a form in which is found, although also insufficiently expressed, the concept about the society of commodity producers in its fully developed and pure form. This is a concept about a society, the production of which entirely and fully is commodity production.[650] And 'the concept about a society of commodity producers, arising from the concept about the expanded form of value, true, is still a very undeveloped concept, but nevertheless [it is] a concept about a fully developed society of commodity producers, rather than a concept about primitive society, having reached such stage of its decomposition, when exchange begins to lose its accidental and elementary character'.[651]

Properly speaking, Kushin, is 'right' when he says that the process of the historical development of society does not coincide with the development of the forms of value, but therewith it is necessary to stipulate that he is right only if we recognise as correct his development of the form of value. The latter in the depiction of Kushin takes a very peculiar character, it is such a development which does not represent any real development, since all forms of value from the first to the last are an expression of the completed commodity society. This kind of thinking has nothing to do with dialectics, this is pure metaphysics; since 'to the metaphysician, things and their mental reflexes, ideas, are isolated, are to be considered one after the other and apart from each other, are objects of investigation fixed, rigid, given once for all'.[652]

For the materialist dialectic, by contrast, it is characteristic that its concepts are mental reflections of the studied material, and the material it is studying in its emergence, development and disappearance, therefore also its concepts are not finished, dead, but flexible, living. Toward the dialectical nature of the studied material veritable science bears a

[650]Kushin 1929, p. 95.
[651]Kushin 1929, p. 98.
[652]Engels 1989, pp. 299–300.

knowledge of the laws of dialectical thinking.

The forms of value, discovered by Marx, are a mental map of the historical and, therefore, the dialectical development of commodity society, beginning with its emergence till its full manifestation. To the development of the forms of value can be entirely assigned the phrase of Engels, stated by him on another occasion: 'the process is a historical one, and if it is at the same time a dialectical process, this is not Marx's fault'.[653]

Kushin in his picture of the dialectical structure of *Capital* tears the dialectic from materialism, the logical process of development of the categories from the historical process of development of the displayed by them phenomena. Thereby creating a picture in a curved mirror, a malicious caricature on the real dialectic of *Capital*.

[653]Engels 1987a, p. 124.

Chapter Twenty-Six

The Assignats of the French Revolution (1883)

Karl Kautsky

People have the habit of fondly portraying the *assignats*, the paper money of the French Revolution, as a fruit of the first French Republic, the Convention and the Directory, and to attribute responsibility for the economic difficulties arising from the mass issue of paper money to the governments of that period. But it is fact that the assignats had already been issued under the reign of Louis XVI, and that the subsequent governments could not suddenly and without further ado leave the road thus taken. The Republic was handed down the assignats of the monarchy – certainly a dangerous inheritance.

We know how the financial difficulties under Louis XVI gave the impetus to the great revolutionary movement which would bring so many momentous catastrophes with it. The rule of the two Louises that preceded him had drained France to the core and the squandering of the income generated by the national labour by the court had reached a level which was downright fabulous. The consequences were inevitable. When Louis XVI ascended to the throne (1774), the state budget showed a regular annual deficit of more than 100 million and the national debt had reached the height of 4,000 million. The government could no longer service the interest on this debt. Taxes were very high and had to weigh heavily on the people, because the nobility and clergy enjoyed in many respects tax exemption. Two-thirds of the lands were virtually tax-free, because they belonged to noble and spiritual lords. Added to this, the collection of taxes was granted to farmers-general, a system highly hurtful to both the state and the people.

So the people sank into poverty, and the governments writhed helplessly in terrible financial straits. The finance ministers were helpless, and the famous Necker could help as little as the swindler Calonne and the haughty Brienne. The financial difficulties brought the king to the momentous resolve to convene first the notables and then the general estates.

The first phase of the revolution broke in, and during the night of 4 August 1789 fell, among other privileges, the tax-exempt status of the nobility and clergy. The financial straits, at first forgotten in the jubilation of the new freedom, soon made themselves felt, because naturally the abolition of feudal privileges could only gradually affect the economic conditions. Looking for new financial resources, the National Assembly decided on 2 November 1789, at the request of Talleyrand, Bishop of Autun, to declare the goods of the clergy national property, while the government took over the payment of the expenses of the Church and its

ministers. On 2 December 1789 the National Assembly decided to sell the goods taken from the National Clergy in order to cover the national debt. Initially, 400 million in goods were to be sold.

In order not to depress the price of the national goods by too large a supply, the French government wanted to sell them only gradually, and decided in the meantime to prepare *certificates* [*Scheine*: notes], which were meant to represent the value of all the national domains for sale. These instructions [*assignats*: *Anweisungen*] were to be used to pay the debts of the state. Those bills were then to pass from the hands of the state creditors, because they had become *paper money*, into the hands of buyers of national property, who would pay with these certificates the purchase price of the national goods. They were meant to be destroyed as soon as they came back into the hands of the state. But that did not happen, at least not to the extent that it should have happened. As Cambon of Montpellier entered the Committee of Public Safety in 1793 and took over the management of finances, he burned forthwith one billion assignats; but neither he continued to withdraw assignats from circulation nor was his example followed by the subsequent governments.[654]

Thus the assignats came into being, and they were certainly a good and skilful expedient invented to help the state out of its urgent plight for the moment. They certainly cannot be regarded as anything more than that. The amount of the means of circulation of a community is in a certain proportion to the amount of existing values and the rapidity of its circulation. Any attempt to increase the amount of paper money [*papierenen Geldzeichen*] above that level must reduce their value, whether their gold backing suffices or not. It is just not possible to arbitrarily turn land or goods into money. The dispute over whether the national goods were able to cover with their values the nominal value of the outstanding assignats is therefore an idle one. That question would only be relevant if the assignats had remained simple mortgage certificates [*Hypothekenscheine*]. Since they became paper money, they had to infallibly decline in values as soon as their amount exceeded a certain level. It did not help that the entire mass of national goods was finally placed as mortgages behind the assignats. The value of the assignats fell in the same proportion as their quantity increased, until they finally dropped to ¼ per cent of their nominal value, so that an instruction [*Anweisung*] for 100 *livres* was only worth ¼ *livre*. On the whole, 45½ billion in assignats where issued, although this amount certainly never was in circulation *at the same time*.

[654]After 9 Thermidor [year II (27 July 1794), which resulted in the fall of Maximilien Robespierre] Cambon received the mock name 'hangman of finances' [*bourreau des finances*], which, however, was in no way justified.

It is of no interest to indicate the individual issues of assignats, because all the French governments behaved in the same way. As soon as money needs made themselves felt, the government stepped in front of the legislative body with the request to be allowed to issue so and so many hundreds of millions in assignats. Approval was never denied, and in this way a colossal amount in assignats was put out. As early as the beginning of 1793 their nominal amount had risen to about 3½ billion.[655]

This flooding of the country with 'revolutionary paper money' brought forth a completely different effect than the authors of this expedient had intended in the first assembly.

One has only to take the external conditions at that eventful period into consideration. All the country was engaged in the struggle. The Republic battled externally against the coalition of European powers, internally against the Vendée and Lyon; the Montagnards fought against the Gironde and Paris fought against the departments. England held France blockaded by sea; all around there were battles, rebellions, executions, arrests, confiscations and conspiracies.

Such times are anything but favourable for industry, trade and employment in general. The young men went off to the fourteen armies that, as Victor Hugo said, Carnot's head had given birth to; agriculture faltered in many places, as well as commerce in the cities. It seemed as if the nature had wanted to come to the rescue of the country attacked from all over Europe, because the harvests were then abundant beyond measure. But trade and commerce languished, the collection taxes went from bad to worse and the government, which at that time not only had to feed its armies but also, above all, feed the population of the city of Paris, then shattered in all its conditions and living as in a perpetual fever. It therefore resorted to the only means that remained to it: by increasing the issue of assignats indefinitely without destroying the ones that had expired.

The consequence of the flood of assignats was a tremendous rise in the prices of commodities. Inflation was general. Commodities disappeared to a large extent from the market because their owners did not want to be paid with paper money; metallic money, which in these circumstances was also a commodity, likewise vanished from sight. The people of Paris would have starved if the government had failed to take all possible measures to give them food. This was done in many cases by means of violent requisitions, because, as

[655]The issue of counterfeit assignats in France was a felony punishable by death. Nevertheless many counterfeit assignats were circulated, which again depressed the value of the paper money. Some governments were not ashamed to print counterfeit assignats and smuggle them into France, so as to help bring about the financial ruin of the country. The English minister Pitt thus manufactured millions of counterfeit assignats. Also in Frankurt a. M. counterfeit assignats were issued and brought by its merchants into France, which, as is well-known, led general Custine in 1792 to impose on that city a harsh contribution.

the government often could only pay with paper money, the owners of the goods also withheld them from it.

While the government thus sought to palliate the people's hunger through bread rations, a wild speculation, in which untold thousands took part, developed in this confused situation, increasing the general misery. Usury also did its part. Despite the sharpest countermeasures this terrible scourge could not be eradicated.

A law which attempted to reduce the disproportion between the value of the assignats and the prices of commodities remained just as ineffective. The government stipulated maximum prices, which were not allowed to be exceeded under the strictest punishment.[656] But this had little effect, because the need to have goods at any price forced the government itself to break the law. A lot of goods disappeared entirely from the market, so that the legal maximum prices for them had to be cancelled. Something similar happened with gold and silver. A law stipulated, upon grievous penalties, that gold and silver could be exchanged for assignats only at latter's nominal value. Then gold and silver disappeared from view, until this provision was again removed.

How much the people of Paris suffered under these conditions is testified to by the frequent uprisings and bread riots. Under the so-called Reign of Terror, the extreme aggravation of the economic situation was temporarily postponed by the iron rigor with which all laws were enforced. But the government remained in anxious concern for the future of public finances, and even in his last speech on 8 Thermidor Robespierre spoke of the all-devouring and burdensome financial system, and called the first two financiers of the Convention, Cambon and Ramel, 'well-known villains', although no reason existed for that accusation.

The travails associated with these manifold laws, the daily assessments, the house searches, the immense tables and their revisions, naturally produced significant discomfort. After the fall of Robespierre, the reaction forced the elimination of all these vexations and popular misery became especially large. The value of assignats, formerly upheld by force, sank ever more. While the course of the assignats had at the beginning been held at 25 per cent [of their nominal value] and still remained under the Reign of Terror at 6 per cent, it now went down to 1 per cent, then to ½ and at the worst time to ¼ per cent of their nominal value. The assignats never surpassed that value under the Thermidorean government and under the Directory. Let us note, in order to give some examples of the disproportion between the value of the assignats and commodity prices, that in 1796 1 Louis d'or in gold was worth in paper

[656]['The two strongest governments which ever existed, the North American revolutionary government and the French National Convention, ventured to fix maximum prices, and they failed miserably' (Engels 1987a, p. 177).]

19,000 livres; a cart-load of wood cost in paper 10,000 livres, a sack of flour 19,000 livres, twelve bushels (= 15 liters) of beans 14,000 livres, the same quantity of barley 7,000 livres. Paris then needed every day 1,900 sacks of flour, and at one time a member of the Council of the Five Hundred, Charles Cochon de Lapparent, calculated that supplying Paris with grain just one month would cost as much as the entire government revenues of France in one year. The calculation may have been a bit of an exaggeration, but it is nevertheless impressive enough.

Under these circumstances, the situation of the rentiers that received their pensions from the state in assignats was necessarily very bad. With regard to private contracts, the Convention had decided that no creditor should have to accept payment of a debt that originated in the period before 1792. But when this provision lapsed, things changed, and to the Council of Five Hundred a case came for discussion, in which someone borrowed 15,000 livres in silver, then later with 15 Louis d'ors bought 30,000 livres in assignats, and with half this total repaid his debt.

The Directory, a government that actually started without financial resources and faced general discontent, made vain efforts to free itself from financial difficulties. About this time it happened that the stock market was closed in Paris to get rid of agiotage, but this measure was unsuccessful. The 'poisonous tree' was very soon reopened.

A forced loan, through which the Directory wanted to get rid of the paper money, failed. The Directory therefore felt compelled to help itself by other means, and made an attempt to drive out the devil with the help of Beelzebub, namely to suppress the paper money with new paper money.

It was assumed that debt-free national domains were still available for 6 million. At the same time it had been calculated that about 24 million in assignats were still in circulation. And thus were created, by Act of 17 March 1796, the so-called *mandats territoriaux* (territorial mandates). These mandates, which were not very different from the assignats, as the same represented an actual value; people could buy with them any national property at the price it had in 1790, when the payment instructions were brought in at their nominal value. It was believed that this paper money would retain its nominal value. Mandates worth 2,400 million were issued, of which 800 were to be used for the redemption of the outstanding assignats. The assignats would be exchanged for mandates at 3⅓ per cent of their nominal value; in fact, their price stood at just ½ per cent.

But the whole project failed and, due to the reasons outlined above, it had to fail. To be sure, the presses for printing assignats were solemnly burned, but a new paper money, albeit more

valuable, had just been introduced in place of the old. At first, the paper money had absolutely no credit. Then people believed that the end of the Republic was at hand, and that the national property would revert to their former owners. Finally, speculation also developed around the new tokens of value [*Wertzeichen*]. In short, the mandates were unlucky and fell prey to devaluation, just like the assignats. They fell, according to a remark by Camus, to 5 per cent of their nominal value. However, the position of the government nevertheless improved somewhat by the fact that the 600 million in mandates issued for the next government expenditures brought about 50 million in silver value to the state coffers.
Change would come not from within but from outside. The General Bonaparte did not exaggerate when he addressed his soldiers in his famous proclamation of March 27, 1796:

> Soldiers, you are naked, ill fed! The Government owes you much; it can give you nothing. Your patience, the courage you display in the midst of these rocks, are admirable; but they procure you no glory, no fame is reflected upon you. I seek to lead you into the most fertile plains in the world. Rich provinces, great cities will be in your power. There you will find honour, glory, and riches.

The fulfilment of this promise also brought the liberation of the Directory from the burden of paper money. Because the soldiers did indeed find honour and glory, but the riches and treasures confiscated by Bonaparte in upper and middle Italy flew to Paris, to the Directory's chest. The victorious general was certainly not left poor; but to Paris flew contributions from Italy, the Netherlands, Germany and the West Indian colonies; victory brought riches. The generals of the Directory were on their own; they had formal instructions on how much they should collect as contributions. Thus it came about that at the end of 1797 the whole issue of paper money stopped and metal money began to rule again in the form of the franc.
It may be true to say that the assignats have nourished the first French Republic. But we must not forget that they were just an after-effect of the errors of the old regime, because governments before 1789 had plunged the country into that immense financial misery. The first National Assembly created the assignats to give financial means to the reign of Louis XVI, and Louis XVI himself confirmed that decision. So paper money was handed over by the Bourbon monarchy to the republic, which, isolated and in struggle with the whole of Europe, possessed neither the time nor the means to suddenly create new resources. But if the assignats partly sustained the Republic, they also did their bit to bring about its downfall. Because the wants associated with the paper system, the embarrassment of the governments, the breakdown of the economic conditions, created a lot of enemies for the

Republic and paved the way for the dictatorship of the sword, for the 'Robespierre on horseback', for Napoleon Bonaparte.

We have neither whitewashed nor concealed, but only depicted what in our opinion were the characteristic traits of this remarkable economic phenomenon, which can help to explain many events of the revolution more than some of the phrases spoken in the Convention and praised by revolutionary mythology.

Chapter Twenty-Seven

Problems of Central Bank Policy (1909)

Rudolf Hilferding

These two articles (the second is titled *Cash payment and Bank separation*) were prompted by the prospect of a separate Hungarian Bank, so besides many interesting general considerations, they also discuss the scenario when an economically weaker national territory tries to split from a currency union. Hilferding looks at the Austro-Hungarian money system as it existed at this time. Convertibility into gold, that is 'cash payment', de facto existed.[657] There was however just no legal obligation for the Austro-Hungarian central bank to do so. Hilferding therefore named the Austro-Hungarian money system a *paper currency*.[658] These articles are rarely mentioned in discussion of Hilferding's money theory, which centre on his example of the restricted silver currency in 1880s Austria-Hungary. Yet his present discussion of the 'paper currency' in early twentieth century Austria-Hungary appears to be just as relevant.

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1. Problems of central bank policy

On 31 December 1910 the privilege of the Austro-Hungarian Bank expires on the exclusive right of note issue in the monarchy. The Bank has posed the request to the governments to renew the privilege, but finds in so doing the resistance of the Hungarian parties, that come forward with the demand of the separation of the Bank. So here intertwine two problems, one of state power politics with another of currency policy. The theoretical examination must of course consider both problems first in isolation.

Today we want to discuss the paper money currency and its laws. So we gain the theoretical basis for the discussion of the questions of bank separation and the adoption of cash payments.

The Austrian currency is according to the law a gold currency like the one in Germany or England. But it differs in a small provision of the one of these countries. The obligation of the Bank to redeem its notes in gold on demand at any time, is – suspended. But since it is the

[657]For details see, per Hilferding's recommendation, Mises 2012.

[658]In any case, Hilferding did not consistently apply this classification, see his 1936 article where he calls the dollar a pure gold currency.

essence of a gold currency that anyone who has money claims, can insist on their settlement through gold money, this provision again suspends the gold currency and since the notes are legal means of payment [*gesetzliche Zahlungsmittel*], so in Austria *paper currency* prevails. The demand to institute cash payment consists in nothing other than that the bank is forced to pay its notes on demand in cash, that is, in gold money. Therewith the question arises as to the meaning of this demand, which coincides with the question of the difference between paper and gold currency. But should these questions be answered, we need to know the economic laws that govern, on the one hand, the paper currency, on the other hand the gold currency. Our first question is thus: How is paper currency possible?[659]

Commodities exchange with each other according to their value, which is determined by the socially necessary labour time contained in the commodities. The intervention of money does not change anything of this law. For the value of gold money is determined by the necessary labour time for the production of gold. But obviously this provision does not apply for the exchange between commodities and paper money. For it is clear that the purchasing power of a 20 krone note is not in any way determined by the minimal cost of printing of the small piece of paper. If the banknote is only a promissory note [*Schuldschein*] on gold, so that everyone at any time by presenting the note at the counters of the Bank will get a golden 20 krone coin,[660] there is nothing strange in the matter. But from where stems the purchasing power of the notes, when the Bank is explicitly released from the obligation to redeem them?

Schoemaker A buys for 20 K a skirt from tailor B. The latter buys for 20 K a pair of boots from A. A has his 20 K again and has in addition swapped his boots against a skirt. The money has changed hands, has gone from A to B and back from B to A – a useless way. The money has functioned as a measure of value and neither A nor B could have specified the price of their commodities, if they had not known the value of money. But this knowledge they could also have had, when they both had possessed not a penny. Money would be for them mere ideal, but already the ideal would have been sufficient in order to be able to function as a measure of value. So one sees, in money matters indeed the friendliness stops, but not the idealism, if it remains only critical idealism. What counted was the exchange of skirt and boots, and in this gold plays only the vanishing role as a representative of value. If A with a promise to pay of 20 K, a bill of exchange, pays to B the skirt and B returned the bill of exchange, when he

[659]Within the narrow frame of a journal article it can be of course only a treatment in the most general outlines. A more detailed theoretical discussion of the problems, which the latest evolution of the currency system present, must remain the reserve of a broader study. (The present work is already for a long time in our hands, but had to be postponed due to lack of space. Editor's note. [*Der Kampf*])

[660][The gold content of a 20 krone (or corona) coin was 6,7751 grams. Two gulden equalled one krone.]

obtained the boots, money would have been spared. Such acts of exchange however proceed in capitalist society incessantly; they must take place, because only thereby the demand fulfilment of society is met. Insofar however as here commodities will be immediately replaced by commodities, money is for the process even *superfluous*; it can thus by conscious convention be thrown out and replaced by *money tokens*. When the state, the only conscious organ available to capitalist society, accomplishes this replacement, it creates a state paper money, which it, since gold has become superfluous, can give legal payment power. So long as state paper money remains limited in its amount only to the *minimum* of gold that would be necessary in all circumstances for the circulation of commodities, it is clear, that it is nothing else but gold tokens. Gold circulates *alongside* this token, in order to satisfy every need beyond the minimum. Let us assume the commodities that circulate required a total of 600 million gulden for their circulation and there would be available about 300 million gulden paper money, so in addition 300 million in gold would have to circulate. It is clear that the paper gulden in its value cannot deviate from the gold gulden, since after all for circulation 600 gulden are necessary, 300 gulden in paper therefore are necessarily needed, paper and gold fulfil here the same functions. Here paper has the the same worth as gold, because it within the commodity circulation performs the same function. It is representative of gold.

The matter could however also be very different. A state wages a costly foreign war, for which large payments are to be made, that, because they head abroad, must be made in gold. The government knows the suitable means, to throw gold out of circulation, by throwing paper money in it. Out of necessity, it seeks to extract all gold out of circulation and far exceeds thereby the minimum. Assume the case that it drives it so far that gold entirely disappears from circulation. What will be the result? We have an up and down ebbing tide of commodities, which now however first confronts a mass of means of circulation far above the minimum mass. Paper money however has no other function than that of means of circulation; it must be entirely absorbed in circulation; gold, which it could represent, is in general not present; by what now is determined the value of the paper gulden? Assume that the sum of commodities, that would have to circulate, is 600 million gulden. We assume also that each gulden serves only once as means of circulation. If paper gulden are issued in the amount of 600 million, then a paper gulden will still be equal to one gold gulden. But if now the sum of commodities falls, so that only 500 million gold gulden would be needed for circulation, then now also the purchasing power of the paper guilder alters. Paper money remains in circulation; but the 600 million gulden can now circulate only commodities of a

value of 500 million gold gulden; the purchasing power of the paper gulden has fallen; instead of the previous purchasing power, that of the gold gulden, it has now only the purchasing power of 5/6 gold gulden. At the same time the determining factor of the value of the paper gulden has radically changed. Previously its value as representative of gold was directly determined from it; this lasted as long as the paper money represented only a portion of the required gold in circulation; now however paper becomes the autocrat; but this autocrat has this in common with others, that its value is only the reflected value of its surroundings; paper has no own value worthy of consideration; it only holds as something in the social relation to commodities, like the despot only in his relation to bureaucracy and military; the purchasing power of paper money is now determined by the sum of the prices of commodities, that it must circulate; whatever is printed on the paper chits, they only hold so much that their total is equal to the sum of the prices of commodities entering in the circulation, which itself is determined in the last instance by the socially necessary labour time to produce them. Why however is not circulation, as it would appear possible at first sight, exclusively attended by the almost costless paper money instead of the so expensive and for that matter useless gold? The reason is: the sum of the prices of the commodities entering circulation is always fluctuating; but therewith also fluctuates the validity of paper money. Instead of an almost stable measuring scale, which is subject only to minor and over a longer period distributed fluctuations, we would have a perpetual oscillation, which would make any calculation, any computation impossible. The constancy of the value of money would therefore be impossible, and so paper currency cannot be brought into harmony with the economic needs.

So if the replacement of gold by state paper money with forced currency is rational only to the extent of the social minimum of commodity circulation, then from the standpoint of economising the precious metal this compensation is insufficient. The circulation of commodities is subject to extraordinary fluctuations both within a year – think of the increase of commodity movement after the harvest – and within the economic cycle; think of the difference between the price sum of the commodities to be realised in the depression and the boom.[661] In addition, it would be for the developed capitalist production an intolerable bondage, if the expansion of production above the attained norm would always depend on the expansion of gold production.

This barrier must be overcome, and it is overcome by *credit money*. A sells a commodity to B.

[661]According to a calculation of the *Frankfurter Zeitung* with only six, though important articles (pig iron, coal, copper, cotton, wheat, rye) the money demand on stocks of 1905 at autumn 1906 prices had risen by no less *than 1,400 million marks* above the stocks and prices of 1901.

But B has currently no money available, pays rather with a promise-to-pay, a three-month bill of exchange. A buys from C and C accepts as payment instead the bill of exchange of B and passes it on to D, from whom he has bought commodities. D has to pay a debt to B, from which he bought commodities and pays them with the bill of exchange of B, to whom so returns his own bill of exchange, after it has circulated the commodities of A, B and C. Here money has been spared, because ultimately the commodity turnovers, from which emerged the bill of exchange, have mutually cancelled each other. Had this not been the case, if D would not have bought from B, then B would had to finally redeem the bill of exchange. But also then the commodities of A, B and C would have circulated without the intervention of money and only the commodities of D would have been paid eventually in cash. The precondition of the circulation of bills of exchange is the certainty that the bill of exchange at maturity also actually is redeemed. It must thus always be redeemable in cash money, as distinct from the state note. The knowledge about the convertibility however is limited, and so the circulation of such bills of exchange finds its limit at the small number of those in the know, that are able to assess the solvency of the signature. It is quite different, when the bill of exchange carries the signature of someone whose solvency is beyond doubt and known to a large circle. It will then be taken without difficulty within this larger circle and can perform circulation services. So the unknown name of the bill of exchange maker must be replaced by one known as solvent in the widest circles and this service the bank note performs. The bank note is nothing else than a bill of exchange of the bank, which the latter puts instead of the bills of exchange of merchants and industrialists. It instead of the commercial bills of exchange deals out its own, the bank notes. Since its solvency is known, so its bills of exchange are taken by everyone. To increase the circulation capacity, it draws up its bills of exchange at round sums, and as it is committed to redeem them on demand at any time, it does not need to pay interest like the merchant, who pays only after three months. The bank therefore discounts to A the bill of exchange of the merchant B, that is, it gives him the same amount in notes, after deduction of interest or a discount for three months. A now pays C in notes instead of in the bill of exchange, likewise C to D and D finally to B. B must redeem the bill of exchange after three months to the bank and pays it with his own notes, that in this way return to the bank. The circulation capacity of these private debt titles is thus based exclusively on the fact that they can be redeemed in cash on demand at any time. This redemption will be to a large extent unnecessary, since the bills of exchange mutually compensate. Yet the bank must always be ready to redeem the bill of exchange in gold, and hold therefore a reserve in gold.

It is known that the state has very often abused the possibility of replacing gold by state paper. As response to these abuses principles of bank policy have been established, that would throw the baby out with the bathwater. It was explained, that any paper money with forced currency [*Zwangskurs*] is bad and dangerous. From money circulation any irredeemable paper money had to be eradicated; each note had to be convertible upon demand into gold. Since one however nevertheless could not pass by on the necessity, to economise gold, so one found a way out in a compromise, like it was first realised in England. One knew namely from experience that a minimum of notes was always held in circulation; so one did not have to fear that for this amount gold would ever be desired; from aversion against the state note this however was in general not permitted; one allowed however the Bank of England, for this amount to issue bank notes without gold backing, while each note in excess of this amount had to be fully covered with gold. But that means nothing else than that the function of the state note has been transmitted to the bank note, while the actual function of the bank note, to satisfy the above the minimum necessary circulation needs, was taken from it and on the one hand transferred to gold, that with any stronger expansion of commodity turnover must flow into the (internal) circulation, on the other hand has been replaced by other forms of credit money and an organisation of payment traffic (cheque and clearing system), before which, although they fulfil exactly the same function as the bank note, the economists did not have that awe [*Scheu*] as before the note circulation. The consequence is the lack of elasticity of the English money system, which would be unbearable, if the bank note would be the only form of credit money and would not be replaced by other forms, which the bank note legislation cannot touch. By contrast, the continental central banks were organised more reasonably. However, one sought also here by law to provide for the note cover. One determined that the issued notes must be covered by one-third or as in Austria by two-fifths of metal, and took the concern, that the bank notes could be issued in excess and thereby devalued – an entirely unwarranted fear, as long as the convertibility of the note is statutory and the activity of the bank is not a fraudulent and reckless one – into consideration by obligating the central bank to a tax at a transgression of a determined note mass, that should force it, to increase the interest rate and thus restrict lending.

So the bank note out of fear of violations by the state has been burdened with the function of the state note. More momentous however was the opposite process, the transformation of the bank note into state note. Whether bank or state note, paper is paper, and paper is patient, very unlike a war minister, who is in need of money. If the state raised once gold, by

fishing it through the issue of state notes out of circulation, then later it made compulsory loans at the large gold reservoir, the central bank. But as the latter pointed out, that if from it gold is taken, no human will voluntarily accept any more its notes, so the state used violence and declared the Bank free of the obligation to redeem its notes in gold; to nevertheless force acceptance of the bank notes, the state declared at the same time, they need to be accepted, because they are *legal means of payment*. Thereby the transformation had succeeded, the bank note, may it also have retained its less blemished name, had become state paper money with forced currency. The cash payments were ceased, namely internally, as the minister of war could pay abroad only with gold bullion.

Here thus the situation of paper currency has arisen, since the metal is drained and immediately the consequences show themselves. The validity of money will fluctuate, depending on the fluctuations of the sum of the prices of commodities entering circulation in case its mass remains equal (constant), and depending on the mass of the spent money in case the sum of the prices of commodities remains equal. In reality the variations will be composed of both elements, mutually reinforcing or weakening themselves. These variations will be the easiest to detect, when one compares the validity of money with gold money of another country. Assume that 100 Mk of the German and 118 K of the Austrian currency contain the same amount of gold; then 100 Mk are = 118 K. If I can always turn my krone notes into gold krone, then also 118 K will be = 100 Mk. It is different however, if too much (or what theoretically under certain conditions is as possible, too little) notes were issued, too much in proportion to the amount necessary for circulation: then I would have to give for 100 Mk perhaps 120 K instead of 118 K. The paper krone is depreciated and this appears in the fact that I must give for 100 Mk 2 more paper krone, then in case I exchanged them against gold krone. The exchange rate, which indicates to me how much the currency of one country is considered in the other country, has deteriorated for Austria by 2 K, or the Austrian currency shows instead of parity, equality of 100 Mk to 118 K, due to the contained in them equal weight of gold, a disagio. The size of this deduction, which weighs on the Austrian money, at the same time indicates the fluctuations in the Austrian money value.

These fluctuations must however be eliminated, since they deprive the calculation of prices first for the import and export, but then also in slowed repercussion for the domestic market of each certainty. How is the elimination possible? The prevailing theory of money provided therefor three conditions: The state paper money must disappear from circulation, the notes at any time be redeemable in gold and hence the bank have a sufficiently large stock of gold available for redemption. To this was still added the self-evident requirement that the bank

was obliged at any time to mint the gold that was passed to it by individuals into gold coin (the so called free coinage). The Austrian currency reform now sought to comply with these requirements. Governments took a loan from abroad, used the proceeds for the purchase of gold and made this available to the bank, by simultaneously withdrawing the state notes from circulation. In contrast, the second condition was not fulfilled; the obligation of the bank to redeem its notes in gold on demand at any time remained suspended, the cash payments were not adopted. Nevertheless, however, the fluctuations of our currency have disappeared; the comparison with the gold currency countries shows that the Austrian currency, although it legally (through the suspension of cash payment) is a paper currency, knows no other fluctuations than those normal ones, also undergone by the pure gold currencies. Here the prevailing theory, that called for the adoption of cash payments as a necessity, was refuted strikingly by practice. Indeed here is a new problem, that contradicts earlier experiences.

The solution of the problem practice itself gives. We have seen that the shortcomings of paper currency consist in the continuing fluctuations of the validity, the purchasing power of paper money. Since paper money has no own value, so it obtains this only as a representative of the respective sum of commodities in circulation and shares in its fluctuations. This can be avoided if the paper money supply is always regulated so that it is exactly equal to the gold money mass, which the mass of commodities contained in circulation required. The task would be unrealisable if it had to be solved for the entire world economy area in general. For no one can at any moment exactly calculate the total mass of commodities present in circulation, their price and the velocity of money. The task is different however, when a comparative scale can be found, that immediately indicates any deviation of the paper money exchange rate [*kurs*] from gold money. And precisely this scale is the exchange rate with the gold currency countries.

Austria stands to gold currency countries in active trade relations, from which continually arise payment obligations and payment claims. Suppose for example, Austria had sold around 110 million krone commodities to Germany and bought around 100 million krone commodities from Germany. The German importers give first as payment to the Austrians bills of exchange to the amount of a 110 million krone, which they paid in marks. But 100 K contain however the same amount of gold as 85 Mk. The Austrians obtained thus for their commodities 93.5 (85 + 8.5) million in mark bills of exchanges, that is in money orders, which are to be redeemed in German gold money. On the other hand, German exporters obtain for their commodities Austrian bills of exchange in the amount of 100 million krone,

payable in Austrian money. The bills of exchanges fall due; German importers now have to pay 110 million krone to Austria; they will look on the German money market for Austrian means of payment. There they will find 100 million krone in bills of exchange, which they will use to pay, since in so doing the payment makes no additional costs; were they to pay in gold, so would arise comparatively considerable expenses by dispatch of gold, that must be insured and during dispatch time of course lies fallow, thus carries no interest. The Germans need not merely a 100, but 110 million krone. As the supply is less than demand, the Austrian bills of exchange will rise in exchange rate [*im Kurse*], that is for 100 K a bit over 85 Mk will be given. But this increase cannot go beyond a certain point. Assume the case, that the cost of sending 100 Mk gold amounted to 1 Mk, then nobody would pay for a hundred krone bill of exchange more than 85 Mk 85 penny. Because if the exchange rate has reached this level, it will become cheaper to pay with gold than with bills of exchange. The exchange rate can in our case not rise above Mk 85.85; this exchange rate would be the upper gold point, that is, the point above which the exchange rate cannot rise, because, if it is reached, the demand for bills of exchange as a means of payment stops and now with gold is paid. The balance, which is thus to be honoured by Germany to Austria from the commercial intercourse, shall be paid in such a way that the Germans on their money market buy the Austrian bills of exchange at a price of Mk 85.85 for 100 K and so pay 100 million krone in Austrian bills of exchange; the remaining 10 million krone they pay in German gold, for which they need 8.5 million marks, whose dispatch [would] cost them 85000 Mk. The exchange rate is thus in this case for Germany unfavourable because the Austrian bills of exchange on the German money market stand high.

The relations are the opposite in Austria. Austria has to pay to Germany 85 million marks = 100 million krone. On the Austrian money market there are however 93.5 million marks = 110 million krone of German bills of exchange. The Austrian exporters who have obtained these bills of exchange for commodities sold to Germany, offer them to the Austrian importers, who can use them to pay for the commodities received from Germany. Here however the demand exceeds supply. The exchange rate will thus sink. The owners of the bills of exchange need Austrian money. They could send their bills of exchange to Germany and let them there be redeemed in gold, bring this gold then to Austria and let it here be remelted in Austrian coin. But this involves costs, they will therefore prefer to sell their bills of exchange to importers, even if the proceeds are less, than corresponds to the parity 100 K = 85 Mk, and indeed they will sell their bills of exchange as long as they for each 100 Mk, obtain their mark bill of exchange 85 Mk less 85 pennies, the cost of sending money, thus Mk

84.15 = K 99.15. For less they will not give up the bills of exchange, because it would be more advantageous for them then, to send their bills of exchange to Germany for payment and let the gold be send to them. The exchange rate [*Kurs*] of Mk 84.15 for a hundred krone bill of exchange in Vienna would be the lower gold point; below this exchange rate the German bill of exchange cannot fall, because at this exchange rate the supply of German bills of exchange in Vienna ceases and German gold would be imported. The rate of exchange [*Wechselkurs*] between gold currency countries has thus for its fluctuations fixed limits, which are given by the upper and lower gold point whose distance in reality of course is much lower than in our example.[662]

The rate of exchange between gold currency countries fluctuates thus only within the limits that condition the cost of effective gold payment. Fluctuations cannot go beyond that, since otherwise instead of credit money the gold money steps forth. It is different when the one country does not have a gold currency, but paper currency.

The relations are easily derived. Suppose Austria would have to make payments to Germany for 200 million krone, Germany to Austria for 100 million krone, which would, with gold currency in both countries, as we know, be equal to 85 million marks. On the German money market there is thus demand for 100 million krone, which faces a supply of 200 million krone Austrian means of payment (bills of exchange). The result would be a decline in the exchange rate. 100 K would not achieve in Berlin 85 Mk, but only Mk 84.15. At this price 100 million krone bills of exchange would be sold and thus meet the demand. The remaining 100 million krone would be sent to Austria for redemption and therefor money would be sent to Germany. However, the Austrians do not pay in gold, but in their paper money. This cannot be used in Germany as a means of payment, but only in Austria. If it is therefore not to become completely worthless, so it must again be thrown in Austrian circulation. The German importers needed however means of payment only for a 100 million krone; that is the amount that Germany can throw in Austrian circulation since it has drawn from it commodities of the same amount; but German exporters want to get rid of their 200 million krone, as they fear otherwise to retain in the hand for them worthless paper chits. Consequently the offer of bills of exchange will certainly not stop, when the rate of exchange is Mk 84.15. The competition of exporters will continue and reduce the exchange rate further. Since however there exists only for 100 million krone = 85 million marks demand for Austrian means of payment, they will obtain only 85 million marks for their 200 million krone bills of exchange. The exchange rate will have fallen to Mk 42.50. The Austrian

[662]Since 1901 in Vienna the exchange rates have never increased by more than 0.2 per cent above parity.

currency is thus, as the exchange rate with the gold currency country indicates devalued by half. The fluctuations in the exchange rate in this case are thus unlimited and only regulated by the changing ratio of demand and supply of the means of payment of the paper currency country on foreign money markets. To enumerate the results of these fluctuations, which extraordinarily aggravate any financial calculation, particularly in trade and industry, is not necessary here. We are interested here in only the one aspect, that the devaluation of the currency, as it appears on the money market abroad, at the same time of course must signify a devaluation of the currency within the country, thus a decline of the purchasing power of paper money. If Austria would have had metal money circulation, so gold for 100 million krone would be flown abroad, to clear the debt to Germany. Now flow to the domestic circulation instead 100 million krone from Germany, but we already know that the proliferation of irredeemable paper money above the scale determined at any time by the circulation must draw the depreciation of paper money in its wake.[663]

At the same time we recognise also the only means to stop this devaluation. It would thereto only have been necessary that 100 million in gold would have been sent to Germany; this necessity was indicated by the sinking of the Austrian exchange rate in Berlin to the lower gold point. And indeed, the whole art to stabilise the paper currency in its exchange rate abroad as well as at home, consists therein *to provide the necessary means of payment for abroad*. The domestic circulation can do entirely without gold money in principle; if the circulation widens, so widens the bill of exchange circulation and therewith the banknotes circulation; if the circulation contracts, so decreases the bill of exchange circulation and the banknotes flow back. As long as the credit of the central bank is unshaken, its management issues notes only against strictly bankable coverage, gold is unnecessary; on the other hand in foreign traffic, where the note cannot be means of payment, but only gold instruction, always the necessary gold must be made available, to protect the exchange rate against major fluctuations.

We have seen that the devaluation of the Austrian currency has occurred in Germany, because the Germans had 100 million krone bills of exchange more than they needed to pay in Austria. These 100 million krone they wanted to turn into German means of payment; it makes no difference in what form they obtain these German means of payment, whether in gold or in German banknotes or in bills of exchange, that can be redeemed in Germany in German currency. For them it is after all only a matter of obtaining German instead of Austrian means of payment. On this rests the so called foreign exchange policy of the Austro-

[663]How such a devaluation, that would express itself in price increase of commodities, would set itself through in practice by the medium of foreign trade, cannot be further pursued here.

Hungarian Bank. If too many Austrian bills of exchange are present in Berlin, so of course at the same time too little German ones in Vienna. In our example only 100 million krone = 85 million marks German bills of exchange will be present in Vienna, but the Austrians have to pay 200 million krone for the purchased commodities; the consequence will be, since these 85 million marks bills of exchange are the only means of payment for Germany, that for these 85 million marks bills of exchange 200 million krone must be paid. But if the bank for the missing 100 million krone makes available 85 million foreign currency, that is mark bills of exchange from its portfolio, then the exchange rate of mark notes in Vienna will not increase, the exchange rate of the krone bills of exchange in Berlin not sink, but the parity will be preserved.

Instead of gold thus also credit money can, if it is legally convertible into money in Germany, be used. It is clear that this foreign currency policy offers great advantages. Firstly thereby the cost of sending money is spared. Secondly the foreign currencies bear interest, while gold in the vaults lies fallow.

This policy consists therefore of nothing else, than that the bank in times, when on the Austrian money market there are present means of payment drawn on foreign countries, or redeemable in gold, above the current demand, buys these and so gradually creates a stock of foreign bills of exchange. But if conversely demand for foreign means of payment on the Austrian money market rises above the supply, then the Bank gives these forth from their stock and thereby prevents the exchange rate rises above the gold point. Theoretically one can imagine that in this way also the sending back and forth of gold in international traffic is eliminated, and practically it can certainly be achieved that the gold shipments become severely restricted, the more so, since the here schematically described foreign currency policy can still be effectively complemented by other measures; the Bank can for example hold a portion of their gold treasure and gold assets abroad, such as a deposit in the English, French or German central bank. This has the advantage that it thereby at any time has also access to means of payment of these countries, apart from its foreign exchange reserve, in the amount of these assets. If it pays with such instructions, so indeed decrease their gold assets, but the shipping costs of effective gold are spared.

That this system, which to have been first carried out systematically in practice is an undeniable merit of the Austrian bank policy, is still very capable of development, if also the other major central banks accept it – in Germany to this question is directed already increased attention – is unquestionable. The avoidance of gold shipments would naturally be

a not insignificant saving of *faux frais*, of expenses of capitalist circulation.[664]

But all these efforts are limited first by a political, then by an economic barrier. The political is that the foreign gold assets of central banks, which after all in reality are more or less state institutions and on whose undisturbed function the circulation and therewith the credit of the state is bound, would be at risk in cases of war. Between England and France for example significant gold shipments take place; they could easily be avoided if the Bank of England held a sufficiently large gold deposit in France and vice versa. Since for various reasons, the balance of England predominates in favour of France, the British assets would likely have to be significantly higher. But with a war of France against England, it would be doubtful whether the Bank of France would really pay this gold deposit on request, if for instance the refusal would hamper British credit and therewith the procurement of war funds. Indeed such procedure would contradict international law. But war takes no consideration on the filaments of law. Nevertheless there can be no doubt, that the means for sparing of gold shipments are still far from exhausted and that hence also the role that gold money plays as world money, can be substantially reduced.

The economic barrier however consists therein that credit money must be convertible into gold at all times, since only this in the last instance is the guarantee of the equality of its exchange rate with the value of gold. Only for a country that in the foreign exchange rate at any time possesses the touchstone for the existence of this equality, is it possible to apparently remove gold from its circulation. Apparently: because the international compensation is performed also for this country in gold money, even if partially in the form of payment through gold claims. The gold indeed does not lie in the vaults of the Austrian bank, but for this it owns claims, that finally must be redeemed with the gold in the vaults of the German, English, French bank.

The advantages of the foreign currency policy are for the Bank insofar limited through the legislation, that the Bank may include only 60 million krone of foreign currency in the banknote coverage. This means that it for these foreign currencies may issue only 150 million krone banknotes, since 60 million is 2/5th of 150; these notes are thus thereby covered according to provision by 2/5th. For the sum of foreign currency in excess of 60 million krone it may put notes into circulation only to the same amount. Can the circulation however absorb more notes, then for the loan of these notes higher interest is paid, than foreign currencies bear, so it becomes more advantageous for the Bank, to apply its means in gold than in foreign currencies, the gold instructions. This legal provision has the purpose, to

[664]It is well-known that the Secretary of the Treasury of the United States, Cortelyon, has suggested a proposal to convene an international conference on the avoidance of international gold shipments.

keep awake the interest of the bank in the purchase of gold.
This circumstance does not change the peculiarity of our currency relations. Gold plays in our internal circulation no significant role and the Bank strives through its foreign currency policy to reduce gold payments also for international traffic. Whether this situation corresponds to all the needs of our economy, whether it requires reform by adoption of cash payments, will be discussed in a second article.

2. Cash payment and Bank separation

We have investigated in the last issue of *Der Kampf* the laws of paper money currency, as far as this was necessary to understand the actual design of the existing Austrian currency. We turn now to the problem of whether by the present arrangement of our money system all requirements that are placed on a rational money system, have already been met, a change in our money constitution would be unnecessary, or whether that provision which distinguishes our money system from that of the countries of Western Europe, whether suspension of convertibility perhaps does mean a defect of our money system. Since however cash payment is significant only for international traffic, this however according to the opinion of the supporters of the existing situation can be provided in much more rational manner by the policy of the Bank if the cash payments remain suspended, we must now study closer this policy and its effects and turn our attention especially to the effects of foreign currency policy [*Devisenpolitik*].
As useful as this foreign currency policy, like we have seen, is, one may not impute and ascribe benefits to it, and to the entire system of Austrian bank policy, any mystical properties, that it does not have in reality. This is done however by those who see in the suspension of cash payment a very mysterious means of power, that would protect the Austrian economy from any withdrawal of its once accumulated gold reserve in much more effective way than is the case in countries subject to the obligation to convertibility.
It is therefore necessary to clarify now the effects of the suspension of the convertibility. Until now we have considered the balance of payments only insofar, as it was determined by the balance of trade, by the ratio of import and export. But the balance of trade forms only *one* item of the balance of payments. This is also – we note only the most important part – determined by payment claims from abroad on Austria, that result from the interest rate obligation on our debt made abroad, both state debts and private debts, from which again counterclaims for in Austria placed foreign values can spring [*entsprechen*]. An important

item also constitute obligations that arise from the sale of Austrian securities, government bonds, stocks, debentures abroad or conversely by buying foreign securities; finally those sums that are transferred, temporarily from one country to another, transfers, that spring from international lending. Assume the case, that in Germany prevailed an interest rate of six, but in Austria of only four per cent, so the funds, that are invested in Austria in the short term or are currently unemployed, will be transferred to Germany, where they bear higher interest. This is a movement that springs from the trend towards evening out of the international rate of interest. This is the transfer of larger sums, whereby an otherwise active balance of payments can be transformed into a passive one, for longer or shorter time, depending on the period in which the interest rate difference remains. Analog money transfers can also arise when domestic money capitalists transfer their money to foreign stock exchanges, because there the speculation is livelier, the opportunities for speculative gains are larger than domestically. This passive side would eventually have to be settled in gold and so reduce the gold treasure of the bank. It is clear that these gold transfers that spring only from the desire of loan capital to flow to the places of higher rate of interest, do not emanate from compelling economic necessity. The situation with them is very different than with those sums, which must be sent abroad to even out commitments resulting from international commodity exchange. Here it is about to a certain extent arbitrary movements of money capital, not about forced payment obligations springing from trade or security purchases. The money capital could remain in Austria, if it would be satisfied with a lower interest rate. Therefore this movement is also subject in a very different scale to the exposure of bank policy. The most obvious is, to retain the sums of money in the land thereby that one grants them higher interest. This is also a frequently selected tool. The bank notices from the withdrawal of money that the balance of payments has deteriorated; it counteracts this by increasing its interest rate. The sums remain in the country or foreign funds are now invested here. At the same time an adjustment of the interest rates has occurred; in Austria, the interest rate has been increased to say five per cent, while the sums flowed to Germany have depressed there the interest from six to five per cent.

The Bank can however also proceed differently. The sending out of money abroad must be done in the form of foreign means of payment; these are after all to be invested abroad. If the Austrian money exporters want to send money to Germany, then they need thereto gold or mark bills of exchange. They can obtain both only from the Bank. If the Austro-Hungarian Bank had to redeem its notes in gold, then the banks could present their notes and send out the gold; since the convertibility however is suspended, this is impossible and the emigration

of Austrian capital money must remain undone. The Austrian Bank does not need through the increase of its rate of interest, which is determining for all lending transactions, to protect its gold treasure; this provides the law and the Austrian economy has been preserved from the effects of interest rate increase at the expense of the loan capitalists, which must renounce striking up the interest rate differential. Of course then the adjustment between the German and the Austrian interest rate can likewise not be done.

But one must not exaggerate this undeniable advantage of the suspension of cash payments. First it should be emphasised in the sharpest manner, that it protects the gold treasure of the bank only against such just described and analogue financial operations. But these usually only involve lesser risk. They are transactions that last only a certain amount of time and provide the assurance that the capitals flow back after some time, thus will exert the opposite effect on the balance of payments. Admittedly they can be made in a time when they could bring the danger of a credit shock in consideration of the situation of the domestic money market. But a permanent danger to the gold treasure they do not form and thus they stand in contrast to the other items of the balance of payments, that result from the movement of commodities or other unavoidable payment obligations, such as for example arise from interest payments for government debt. If these items desire for example the adjustment of a favourable balance of Germany, then these *must* be settled, and namely in German means of payment; if these would now be denied by the bank, then the mark bill of exchange in Vienna would rise rapidly above parity, in Berlin the krone bill of exchange fall below parity. In case it had been mere financial transactions for exploitation of the interest rate differential, the rise in mark bills of exchange would have prevented the export of gold; for the higher cost of purchasing German means of payment would have swallowed the profits of the banks from the higher interest rate. Now, however, the payment obligations must be met, if the belated debtor should not be declared bankrupt. If the German means of payment now were not available, then the devaluation of our currency would become obvious. The Bank is thus obliged, for these purposes, just as gold, to make available respectively gold instructions on German locations, just as if it paid in cash. It are however only such, perhaps suddenly occurring shifts in the balance of payments, which may pose a threat to the bank, if they continue. So a significant deterioration in the balance of payments by an alteration of the balance of trade could occur as a result of crop failure, which forces us to import cereals in large quantities, instead of exporting. The deterioration in the trade balance, if no other items exert an opposite effect, would have finally to be evened out in cash gold and the Bank would have to make available the necessary cash money (gold). Likewise when for instance a

stronger return flow of securities from abroad would develop and therefor large payments would have to be made. Any refusal by the Bank to meet this payment by submission of gold would devalue our currency immediately. Here then the suspension of cash as a means of protection of the gold treasure fails completely and the bank must act exactly as if it were a cash paying one. To protect its treasure it can then just use the same means as any cash paying bank, must thus finally take recourse exactly in the same extent to the increase in discount, to attract foreign capital, to push the price of securities and therewith counteract the return flow of these.

But the virtue of the suspension of cash payment will furthermore be reduced by the fact that it also in the case, where it represents an effective means of gold protection, can be replaced for the most part by others, which the cash paying bank may also use, though of these means is generally spoken little. Here belongs especially the gold premium policy of the bank of France, of which the 'metallists', the dogmatic gold currency politicians, have so great disgust. Since in France not only gold but also silver coins are legal tender, the bank can redeem its notes both in gold and in silver franc coins. If one wants the redemption in gold, then the bank may desire a surcharge and this premium is usually enough to prevent the export of gold. Other banks help themselves in others ways. Apart from the minor arts, such as redemption of notes in already heavily by circulation worn coins, that can be used for export only at a loss, since on the world market gold is measured only according to weight, the central banks use their predominant position in the credit organisation, to prevent gold exports by the banks and big money traders, for instance by the threat, to meet them less when discounting their bills of exchange or with other credit operations. All of these measures of are also effective, but only under one condition: the status of the balance of payments must be such that an outflow of gold is not indispensable to settle committed obligations. The central bank can thus by such a policy, which leaves the interest rate unchanged, only prevent the outflow of gold, if it springs from purely financial transactions. Does for example a bank of a country whose interest rate is 3 per cent, want to invest 10 million francs in another country, because there the interest rate is 5 per cent, and can it, due to the level of the rate of exchange, make this investment only in gold, then any central bank can prevent such gold exports; the Austrian Bank will simply refuse the submission of gold and can do this due to the suspension of the redemption obligation without further ado; the Bank of France would demand such a gold premium, that export becomes unprofitable despite the higher interest rate abroad. The German Reichsbank would have it somewhat more inconvenient; but it would tell the gold exporter in a friendly conversation that their

weakening of the gold treasure would at this moment be undesirable and the gold exporter knows, that it would be unwise, to provoke the irritation of the powerful central bank. The Bank of England however – will give the gold, for the simple reason, because in its board of directors the influence of the major gold dealers predominates. It is thanks to this fact that London is the only truly free money market, which has however for London also the advantage of remaining the centre of the gold market and the gold trade in the world.

Undoubtedly this policy is effective. Proof of this gives the difference between the discount rates of the various economic areas. With high mobility of money capital the diversity of national discount rates would have long evened out to a world market rate, at least this difference be far lower, if the 'national' policy of the different central banks would not be able to prevent this adjustment. The greatest significance comes to the Bank of France with its immense amassment of gold in its vaults.

But this policy has its specific limits. So effective it is with purely financial transactions, so it fails immediately when it comes to gold movement, that arise for cash payment of incurred debt obligations on the international commodities or securities movement and so on. The difference is clear without further ado. A gold export of 10 million Swiss francs for finance purposes will be waived, when the central bank by one or other means does not release the gold to the gold exporter. A demand for foreign bills of exchange will however then likewise not take place; the gold exporter will refrain entirely from gold transmission; because his demand for bills of exchange would drive the exchange rate to such height, that the export would be worthwhile as little, as if he would for instance have to pay a premium demanded by the central bank. It is quite different however, if for example the Paris merchants for British commodities delivered to them would have to make payments of ten million francs and these ten million represented the passive side, that would have to be evened out for the Anglo-French trade balance. These ten million *must* be paid, whereas the gold transfer for exploitation of the difference in interest rates could also just be omitted. The Parisian merchants will thus first exercise demand on the money market; the exchange rate would rise quickly above the gold point; if the Bank refused also now the deliverance of gold or raised its gold premium ever higher, then the exchange rate would rise ever more above the gold point, which however signified nothing else than a devaluation of the French currency, whose prevention after all must be the goal of any organised bank policy. That the gold premium policy in France usually prevents the gold export, is simply explained by the fact that the balance of payments of France is always active, so that almost always gold exports from France serve only purely financial transactions. It is only this circumstance which

allows the gold premium policy of the Bank, just as it explains the accumulation of gold in the vaults of the Bank and the meanness and the constancy of the French discount rate.

The accuracy of this exposition has been downright confirmed experimentally by the events in the money market in late autumn 1907. The German Reichsbank made the attempt by pressure on the banks to refrain them from gold exports. First, with success. Soon, however, the exchange rate on London, Paris and so on, rose over the gold point[665] and immediately abroad voices were raised that the German currency had ceased to be a gold currency and that the fluctuations of the German valuta went beyond that of a gold valuta. There was left for the Reichsbank nothing else to do, than by delivery of gold bring the exchange rate back to the normal level, if the incipient distrust in the German currency were to be chased off and thus the disruption of German credit abroad be prevented. Exactly the same thing happened however to the Austro-Hungarian Bank, when it simultaneously made use of its power, not to render cash payment, [in a way] that did not entirely correspond with the money market conditions and did not make available foreign currencies in an amount satisfactory to demand. Also this had a rise in the exchange rate over the gold point as a result and already one could believe, that the long vanished gold agio again loomed. The release of foreign currencies in gold [that is foreign coins] made an immediate end to this situation.

But also the prevention of gold exports with purely financial transactions encounters a limit in the magnitude of the difference of the interest rates. If the difference surpasses a certain degree, so that the gold transmission also remains profitable when the exchange rate goes over the gold point or, what amounts to the same thing, also the increased gold premium can be paid, then also here gold export will have to occur, if the fluctuation of the currency is to be kept within normal limits. Then the listed tools of bank policy fail to prevent the export of gold and there must occur an elevation of the interest rate. This explains for example, why the Bank of France with the elevation of the American, English and German discount rate in late autumn 1907 also in its turn had to proceed with an elevation of the interest rate, to protect its gold holdings by the reduction of the difference between its own and foreign rates. In all other cases however, where the gold outflow evens out only a payment obligations induced passivity of the balance of payments, each prevention of gold export could be bought only at the cost of a devaluation of the currency, it would thus mean the frustration of precisely that purpose, which the amassment of gold serves. It would mean thwarting the function of gold for the sake of the gold fetish. In all these cases, an outflow of gold can only be counteracted by increasing the discount rate, which is always the statutory power of the

[665]The London sterling exchange rate of 20.60 at the time towered above the parity by 0.83 per cent, the gold point by 0.50 per cent.

central bank, whether the bank is a cash paying one or not. The increase of the discount rate attracts foreign capital into the country, reduces the price [*Kurs*] of securities and so prevents the return flow of securities from abroad and thereby a sudden and serious deterioration in the balance of payments, to mention only these important effects of the discount [rate] hike on international gold traffic.

The suspension of cash payments and also the foreign currency policy of the Austro-Hungarian Bank, as helpful and efficient the latter in itself is by economising useless gold transport costs, has thus not that significance for the reduction and keeping low of the interest rate, which some exaggerating admirers of the bank policy attribute to it. It is by no means capable of eliminating the international influences, that act determinedly on the configuration of the exchange rate and therewith on the rate of interest, or even only modifying their effect. Just as little the gold policy has any significance for the configuration of those factors that determine in the domestic economy the interest rate, because for the interior the specific characteristics of the Austrian bank policy cease and the Bank here must follow exactly the same principles like any other, if we disregard the legal mischief of the Peel Act and the American note coverage rules.

After all this the conclusion is easy to draw on the significance of the question of the suspension of the cash payments. What is really done by this authority, the prevention of purely financial gold transactions, other banks can do by virtue of their power position in the credit organisation in the same way. And precisely the Austrian Bank has through the systematic development of the foreign currency policy such a position on the exchange market, that a thwarting of its intentions by private gold arbitragers is not to be feared. The cancellation of this authority would thus remain without influence on the actual configuration of the discount policy of the Bank.

The question of the suspension of cash payment can therefore as such be treated with greater serenity. Seen just from the standpoint of the valuta policy, the retention or abolition of this provision is a matter of indifference. When therefore *Hungary* calls for the removal of this provision, then *Austria* has as such not the slightest reason, for the retention of any one concession, to bring any one offer. As the Hungarians are the demanding ones, they rather must for the fulfilment of their demand make concessions.

But the question of cash payment has also importance in another respect. As long as the Austrian valuta is not also legally a pure gold currency, the credit, which Austrian securities enjoy abroad, is not that of the pure gold currency countries. It misses under these circumstances the absolute certainty that the commitments, that have to be met in Austrian

currency, will always be fulfilled in gold. This effects however, that the demand for Austrian securities abroad is not so strong, as when these securities constitute pure gold obligations. The exchange rate of Austrian papers abroad is thus lower during the suspension of cash payment, than it would be with the adoption of cash payment. This is however a disadvantage because it increases the interest sum to be paid to other countries, a disadvantage, which is not offset by a corresponding advantage. For this reason, maintaining the suspension would be a useless harm, whose elimination admittedly lies even more in the interest of Hungary – due to its greater use of external credit – than in Austria's.

But the question of the adoption of convertibility is today complicated by the fact that it must be linked with another one, with the question of the *bank separation*, the establishment of an independent Hungarian central bank.

That Hungary demands the bank separation would remain incomprehensible if this measure were to be considered in isolation. For it is without a doubt that the commonality of the Bank is beneficial for the Hungarian economy, and this was unanimously admitted by all the experts that have been heard in the Hungarian bank inquiry, wherewith we admittedly do not count to the experts the Magyar independence politicians. The commonality of the central bank means the unity of the Austro-Hungarian money market, means hence, that the Austrian loan capital is made available to the Hungarians on the same terms as to the Austrians. The still predominantly agrarian Hungarian economy is provided for its industrial development with the Austrian capital wealth and this causes the interest rate in Hungary to be lower than it would be if the Hungarian money market did not form a unity with the Austrian one. Conversely, the same circumstance causes the interest rate in Austria to be higher, than if Hungary did not form a part of the Austrian money market.

The configuration of the Hungarian balance of payments works in the same direction of increasing the interest rate. According to the reliable calculations of Gaertner[666] the balance of payments in Hungary looks like this: On the asset side [*Aktivseite*] stands the surplus of the trade balance with 40 million krone, that is, Hungary exports by this amount more abroad (with inclusion of Austria), than it imports; then the precious metal production with 13,54 million krone, and finally the remittances of emigrants to their relatives in the homeland with 100 million krone. The assets side, indicating the amount that Hungary has to receive from abroad, is thus 153,54 million krone. Opposite it stand on the liabilities side, indicating the payments which Hungary has to fulfil to other countries, the following items:

[666]Gaertner 1907, pp. 391 and following.

Payments of the state	206,757 million krone
Interest of ground debt	112,312
Debt of private railroads	21,345
Commodities debt	16,177
Interest from other stocks and bonds	10,07
Withdrawal through emigration	45,00
Sum . . .	411,661 million krone

If one deducts of these liability items the assets with 153,54 million krone, so eventually remain as liability items of the balance of payments the amount of 258,121 million krone. There thus would have to flow out every year about a quarter of a billion krone in gold to foreign countries, to compensate the deficit. This is of course impossible and so Hungary must annually borrow a sum in the specified amount from abroad. This is done when a part of the in Hungary made expenditures of the state, of the industrialists, merchants and landowners is defrayed with money, which by selling abroad debt instruments, bonds and shares, mortgages etc. flows from it to Hungary. Thus Hungary procures the capital for the development into an industrial state. Most of this capital for the Hungarian economy is raised in Austria. On the Austrian money market however Hungary has a preferential position, as long as the unity of the economic area – and this includes the money market – is preserved. It is part of the economic homeland and its securities enjoy substantially the same credit as Austrian ones. This changes in the moment of a separation of the Bank. An adverse balance of payments constitutes a certain latent danger for the maintenance of cash payment. Austria without Hungary has a highly active balance of payments, for itself alone it has not to fear the danger of money withdrawal, which could eventually devalue the currency. With the communality of the Bank the passive balance of Hungary is thus pretty compensated by the active balance of Austria. It is different when Hungary constitutes an independent money market. It must then make efforts to secure the influx of a quarter of a billion of foreign capital annually and prevent, that the gold accumulated in the Bank flows away. Since this gold outflow arises from mandatory obligations of the balance of payments, it cannot be otherwise prevented than by the fact that foreign capital is attracted to Hungary by appropriate height of the interest rate. The independent Bank thus for Hungary means under all circumstances a rise of the interest rate above the level that the common bank can follow.

On the other hand however, the possibility to uphold the Hungarian currency must be allowed even with an independent Bank, at least under normal circumstances and with honest management of the Bank and the state finances. Certainly the passivity of the balance of payments entails dangers with it. Above all one usually emphasises the danger of a strong and sudden withdrawal of money through the reverse flow of securities held abroad, if the Hungarian credit abroad is shaken by some adverse circumstances. But a vigorously and timely applied discount rate increase offers also against such contingencies extensive protection. Increasing the interest rate lowers the price of the securities on the Hungarian market and the low price refrains the foreign owners from selling the papers in Hungary. The restriction of credit makes it on the other hand difficult for Hungarian merchant banks [*Effektenhäusern*] to buy these securities.

Likewise it depends only on the granted height of the interest rate whether the international market [*Ausland*] provides the necessary new capital.

The increase of the interest rate is however for the Hungarian economy a significant calamity. It contradicts also the *fiscal* concern, since it raises the interest charge the state bears for its bonds; the *agrarian* concern, since it increases the mortgage rates, depresses the price of the ground and soil and therewith narrows also the indebtedness limit and hinders improvements; the *industrial* concern, since a larger part of the industrial profit must be paid away as interest and ultimately the concerns of *all classes of people*, since the increased interest flows abroad and therewith a part of the in Hungary produced profits is lost for the industrial advancement of the country.

The separation would work conversely in Austria; to Austrian capital, which is lent to Hungary, would accrue higher interest, while in Austria itself the interest rate would be lower; both would promote industrial accumulation in Austria with a simultaneous rise in land prices and agricultural credit accommodation.

The disadvantages, which arise for Hungary from the increase in the interest rate, create however a danger. With the power of big landowners and big capitalists over the Hungarian government it seems the possibility is not excluded, that, in order to avoid the increase in interest rates, the discount policy is not followed vigorously enough, that the gold outflow consequently reaches dangerous dimensions and finally cash payments are suspended, that means however under such circumstances, that the gold currency collapses and the pure paper money economy steps in its place with all its consequences for the devaluation of the currency. With the size of the Hungarian debt obligations to Austria that would mean large losses for the Austrian capital, which would now receive its claims in a devalued currency. On

the other hand this devaluation would mean an export premium for the Hungarian products, especially agricultural products, that are paid abroad in the full-valued money, while the Hungarian producers would still continue for a long time to pay wages and raw materials in the devalued currency; simultaneously a restriction of imports to Hungary, since the foreign producers have to reckon with the risk that their commodities will get paid in a fluctuating, to ever progressing devaluation tending currency.

Despite everything one should not overestimate this danger. Precisely because Hungary is necessarily dependent on the influx of foreign capital, it must seek to maintain its credit abroad and not cut off all possibilities of industrial development for itself by destroying its credit through deterioration of its valuta. Precisely in the stage of a half-mercantilist epoch, in the striving epoch of state promotion of industry the tendencies to maintain the gold currency will probably assert the upper hand.

If however this understanding is correct, then Austria has nothing to fear from the Bank separation, to expect from it only advantage. To grant any concessions for the preservation of the commonality, would hence be a completely irresponsible and foolish act, that would run absolutely counter to Austria's interests. It is a different question, however, when the Bank separation is not considered in isolation, but as a preparation to total economic separation of Hungary from Austria. And only as such the demand becomes understandable. To the Hungarian economic policy makers the disadvantages of the Bank separation appear bearable, because they hope, that they will be more than offset by the advantages of the independent customs territory. The higher interest rate loses its terror compared to the increase in profits, which the Hungarian protective tariffs should bring, the tribute to foreign capital seems less cumbersome in light [of the prospect] of the exclusion or restriction of foreign industrial competition. That however the commonality of the Bank with a split of the customs territory becomes an impossibility, is clear to even the humblest Hungarian. For even after the experiences that one has made with the surrender of Austrian interests by the Austrian Government – one think merely of the national treason and violation of the constitution of the Ministry of Badeni-Bilinski [1896?] – it must be considered as excluded that Austria through the common Bank would also still provide the necessary money capital cheaper and make more widely than would be the case with a Bank separation, to a Hungary whose independent economic policy is aimed primarily against the Austrian industry. Because however the establishment of the independent economic territory also for Hungary signifies a dangerous experiment and crisis-like shocks during the transition period, it is in the interest of Hungary, not to let two economic experiments coincide, but to move the

separation of the Bank and that of the customs territory to different dates. That is indeed why the Hungarians at the last settlement insisted on the exclusion of the Bank question, a concession, which the frivolous Korytowski has conceded to them in addition to everything else, and that is why they then demanded so emphatically the independence of the Bank. But if the foreign investors are not be overly suspicious against this independent Bank of an economic territory with a passive balance, then the Hungarian Bank policy must be brought into conformity with that of the major European central banks. Abroad one has after the favourable experiences with the policy of the Austro-Hungarian Bank, up to a certain extent become accustomed to see in the suspension of cash payment more a means of valuta policy than a fundamental departure from the basics of the gold currency, which indeed is almost certainly correct. The more so, as abroad one cannot put any reasonable doubts in the eventual resumption of cash payments. But this confidence the independent Hungarian bank would be lacking and hence the demand of the Hungarians to resume the cash payments. But because of that however also this policy measure must be regarded only as a step to facilitate the secession of Hungary and therefore call forth the same resistance, which social democracy in the interests of the standard of living of the Austrian proletariat and in the interests of industrial development must put up against any fragmentation of the economic territory.

The decision of the Bank question cannot therefore be taken only along the principles of the bank policy. Were the Bank question posed by itself, the Hungarians would had never raised it and the Austrians would not need to hesitate in answering. But like this the bank policy is only one component of the policy, that must decide the relationship between Austria and Hungary in general, only a part of the economic policy on which the proletarian interest demands only one answer: not division, but unification, not loosening, but strengthening. So also the decision on the bank question turns into a political one and therewith into a question of power. The unity of the economic territory is impossible under continuance of the dualism; it is only to be secured by achievement of democracy and national autonomy for the whole extent of the empire. To Andrassy, the Minister of pluralities, cannot be conceded the [legal] resumption of cash payment.

Chapter Twenty-Eight

The Pound and the Dollar. Britain and the United States in Struggle for Domination on the World Money Market (1925)

Fedor Kapelusz[667]

One of the greatest events on the world money market[668] that occurred in the second half of 1924 and in the beginning of 1925 was the rise of the exchange rate of the pound almost to the pre-war parity with the dollar, that is, with gold. Let us note in brackets that the restoration of the parity of the currency exchange rate, of course, does not at all mean yet a restoration of the pre-war level of commodity prices. This convergence of the pound and the dollar in its turn posed the question of the return of Britain to a gold currency, factually cancelled since the time of the world war, and moreover is connected with the problem of the rivalry of Britain and the United States for hegemony on the world money market. Before the war Britain was the universally recognised power in this domain,[669] London was the strongest money centre, the world clearing house; after the war the domination passed to the United States, becoming from a state-debtor a state-creditor and amassing more than half of the whole world reserves of gold. The problem of this acquires especially political interest; we can call it the problem of currency imperialism. Besides this, there is connected with it a series of extremely important theoretical and likewise practical questions on the role of gold, on the 'revolution of the value of gold', on the so called superstition of gold, on 'managed currency', as a 'scientific means of fighting with the fluctuations of the market under individualistic capitalism'.[670]

The offered work, of course, does not pretend to cover these difficult problems in their entirety. We will be satisfied, if we succeeded to at least mark the problems and give a cursory

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[667][Kapelusz (Odessa 1876 – Moscow 1945) already in 1897 wrote an article-series in *Die Neue Zeit* on imperialism and finance capital.]

[668]['This includes the bill of exchange market; in general, the loan market; therefore dealings in money, bullion market. As *money-lending market,* it appears in the banks, for instance in the rate of discount: loan market, bill brokers, etc.; but then also as the market for all *interest-bearing bills*: state bonds and the share market. The latter fall into larger groups.... Miscellaneous in infinite variety, such as enterprises of industrial or commercial companies based on shares. Finally for securing the whole, *insurance shares* of all kinds.
Just as the market by and large is divided into home market and the foreign market, so the domestic market itself divides further into market of home shares, national funds etc. and foreign funds, foreign shares etc. But this development really belongs to the world market, which is not only the domestic market in relation to all the foreign markets existing outside it, but at the same time the domestic market of all foreign markets as, in turn, components of the home market' (Marx 1986b, p. 210).]

[669]'The money market – is the most interesting of all markets, because it is world-wide to a greater extent than the market in anything else, with the possible exception of wheat' (Withers 1909, p. 85). The book of Withers is outdated for our time (the 1923 Russian translation was evidently based on the first English edition of 1909 and not even on the 1914 edition), but it gives a picture of the prewar dominance of Britain on the world money market, and likewise of the British banking technique and bank business.

[670]Professor Keynes [no exact reference].

summary of economic material; gaps and mistakes with this are inevitable.

1. The Napoleonic wars and the world war

The depreciation[671] of the pound sterling during the time of the world war and in particular after it had already a precedent in history, namely during the time of the war of Britain with the French Republic and with Napoleon. The official, standard 'price' of gold, namely £3 17s. 10.5d. for an ounce, was established already two hundred years ago, in 1717. Earlier the content of gold in a guinea corresponded with a price of 20 shilling, but at the end of the seventeenth century the guinea on the free market was estimated already as 30 shilling; the victories of [general John Churchill] Marlborough, exhaustion of foreign countries and the measures, taken by the British government for the uplift of its credit, called forth a quick rise of the exchange rate of the pound, and the price of the gold guinea in pounds fell; in 1717 it was agreed to fix it at 21 shilling, this price also was the calculation of £3 17s. 10.5d. for an ounce of gold. Later the convertibility into gold was suspended in 1797 as a result of the war with France, and in 1821 it was restored precisely at the old price of £3 17s. 10.5d. This price lasted until the world war. During the latter Britain, although formally the free convertibility into gold was not suspended, factually introduced a paper currency, banned the export of gold from the country[672] and made with this the convertibility illusory;[673] likewise was banned the sale of mined gold on the open market, free coinage factually disappeared, gold producers were obliged to hand over gold to the Treasury at the rate of 84s. 11.75d. for an ounce (the old official rate of £3 17s. 10.5d. amounted to 77s. 10.5d.). The commission, appointed to deal with the complaint of the gold producers over the too low price, not corresponding with reality, drew the conclusion, that 'for gold can not be paid more, than the value of money'. This is the typical theory of the nominalists, that not gold determines the value of money, pound sterling, but the opposite.

Let us give the comparative table of the depreciation of the pound in the period of the

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[671]'In general the most dangerous period of paper money is not that of its domination, but that of its reduction [when one proceeds towards the restoration of the money currency]' Friedrich von Gentz (collaborator of Metternich) [Gentz 1839, p. 344]. The table given below illustrates this.

[672]Even the United States formally banned the export of gold from September 1917 to July 1919.

[673]In order not to break the appearance of the law on gold coverage of the banknote, there were created parallel to it so called *currency notes*, special war paper currency, bills of 1 pound and of 10s., factually serving [as] substitutes cheques in small daily payments. As is known, the development of the cheque in Britain in the nineteenth century made the role of the banknote of the Bank of England in quality as a means of circulation wholly secondary.

Napoleonic wars (according to Jevons[674]) and in the period of the world war. The numbers given are annual averages.

Year	Price of an ounce of gold £. s. d.			Depreciation in per cent	Year	Rate with dollar (parity 4.866)
1801	4	5	0	8,25	1915	4,75
1802	4	4	0	7,5	1916	4,75
1803–9	4	0	0	2,5	1917	4,75
1810	4	10	0	13,34	1918	4,75
1811	4	4	6	8	1919	4,43
1812	4	15	6	18,5	1920	3.66[675]
1813	5	1	0	23	1921	3,85
1814	5	4	0	25	1922	4,44
1815–6	4	13	6	16,75	1923	4,57
1817–8	4	0	0	2,5	1924	4.41[676]
1819	4	1	6	4,5		
1820	3	19	11	2,5		
1821	3	17	10,5	0		

As in the time of the Napoleonic wars, also in the period of the world war there was created in British parliament a committee for the struggle with the depreciating currency: the so called Bullion Committee and the Committee of lord Cunliffe. When in 1810 the mentioned Bullion Committee proposed to reduce the issuance, parliament rejected this, and the pound continued to fall. Only after some years there was appointed a new committee and there was agreed to move to convertibility into gold: from 1 February 1820 at the price of £4 1s. an ounce, wherewith were allowed only dealings of a minimum 60 ounces, with a gradual decrease of this price to the standard (that is £3 17s. 10.5d.) on 1 May 1821. In his testimony before the mentioned committee Ricardo developed his idea of the quantity theory of money, which also was put as the basis of the Bullion Report. Marx in his theory of money rejects the idea of Ricardo and draws on the material of Tooke. It is understood, we cannot dwell here on these purely theoretical and extremely difficult problems. We are interested, mainly, in

[674]Jevons 1884, p. 139.
[675]In February 1920 the exchange rate of the pound amounted to 3.20 dollars. This was the minimum. The price of an ounce of gold went to £6 2s. 4d.
[676]In January 1924 the pound sterling was quoted on the New York market at 4.21, in June 4.32, and afterwards occurred its rapid rise, and in January 1925 it reached already 4.81 dollars, that is only half a per cent behind parity.

concrete facts. The proponent of the 'banking theory of money' Macleod reports the following interesting facts; in May 1819 five hundred bankers, merchants and the like, filed a petition against the reduction of the issuance, they feared from it harmful effects for the economic life of the country; but when the government went ahead to the restoration of convertibility and with this goal were procured 2000 gold ingots of 60 ounces, then from them in reality only 13 were used, the demand for gold immediately fell, and the government was in a condition to pay the Bank of England upwards of 10 million pounds; as a result the full convertibility into gold, that is without the above-mentioned limitation of dealings of 60 ounces, was restored already in May 1821 instead of 1823. The money mass in circulation was greater in 1822, than in 1819, but a depreciation did not take place. Thanks to the restoration of convertibility, the British government could in 1823 reduce the interest rate for almost a quarter of the whole state debt, that drove to horror already Swift, Hume, Pitt the Elder, [Charles James] Fox and Burke and that in particular increased in the time of the war with France (from £127 million in 1774, to 920 million in 1816). Thus, in 1823 the five per cent navy annuities (Five Navy) were converted into four per cent annuities, and the four per cents were reduced to three and a half per cents. Let us still indicate, that from all the classics only Malthus represents an exception in the sense, that he categorically was in favour of state loans; this is explained by the fact that he represented predominant agrarian interests. Malthus warned against too quick repayment of state debt, and likewise against deflation, since it, increasing the value of money, does not decrease, but precisely increases the relative burden of debts. In our time a similar argument is exhibited by Keynes. Keynes emphasises that under a transition to gold, and in particular with an appreciation of it, the real burden of the colossal domestic debt of Britain automatically increases, the real burden of taxpayers, whereas state income together with prices falls.

In his memorandum on 'The problem of the gold standard' given 18 March 1925 in the Commercial Committee [of the House of Commons], Keynes also drew the parallel with the time after the Napoleonic wars. He emphasises the minuses of that time, as a result of the restoration of gold currency.

> Then, as now, vicious war finance was allowed to breed inflation and virtuous post-war finance to breed deflation. Then, as now, the orthodox party proclaimed that the one thing necessary was to restore gold convertibility; and a little more than a hundred years ago the deed was proudly done. The results were shocking. We suffered twenty years of successive credit maladjustments and crises, the most disturbed and

> troubled we have ever known, barely escaping revolution. The growing discontents of the business world culminated in the famous reform embodied in the Bank Act of 1844. The peculiar Act is largely responsible for the myth about our having an automatic gold standard, which persists in the newspapers to this day.[677]

Undoubtedly, Keynes's judgement is not without bias and partiality. American authors with the same categoricalness, on the contrary, sing praises for the gold standard.

> The election of 1896 – we read in Benjamin Anderson,[678] – with the triumph of the gold standard, is generally looked upon as a turning point in our economic history. It was preceded by years of economic distress, a very substantial part of which was due to uncertainty regarding our future monetary standard. It was followed by a number of years of extraordinary prosperity, a very substantial part of which was due to the removal of these fears regarding our money.

Keynes tries to use the post-Napoleonic period in the spirit of his theory of managed currency and the omnipotence of the credit and discount rate, about which we will speak below; just as Cassel, he boils down capitalist crises exclusively to credit, to monetary reasons. However, also among the British economists of the 1830s and 1840s there formed two schools, of which one (the school of lord Overstone, Torrens, and others) ascribed crises to insufficiencies of the British system of money circulation, while the other (school of Tooke and Fullarton) rejected any kind of connection between phenomena of the one and the other kind.[679] In the same Tugan-Baranovsky the reader meets two opposing viewpoints about the then post-war period, although on a different plane. On one side, he emphasises, that the general position of British industry in the first decade after the conclusion of peace was very difficult, prices of the majority of commodities strongly fell, industrial crises called forth a reduction of production in all branches of industry, the reckonings on increased export to Europe did not materialise, and the workers under influence of needs reached to open uprisings; strongly suffered also the agricultural classes from the fall of prices for their products. But, on the other side, Tugan-Baranovsky comes to the opposite conclusion, that the viewed period was for Britain a time of rapid industrial progress, that the main reason for the fall of prices of manufactured goods was, without doubt, the improvement of technology

[677]Keynes 1925c (1981, p. 339).
[678]Anderson 1925, pp. 24–5.
[679]Tugan-Baranovsky 1923, p. 34.

of production – consequently, let us emphasise, not at all deflation and in general no factors of money circulation. The contemporary uprisings of workers were uprisings against machines.

But the most significant of all is the following: for the years 1821–25 on the London market were concluded foreign loans for the huge sum of £49 million,[680] this together with the conversions [of debt] indicates the abundance of available money capital. Tugan-Baranovsky, evidently, is inclined to associate this with a stagnation of sales, but we emphasise this phenomenon, as an indication that even in that epoch of the greatest rise of British industry, the epoch of technological revolution, in Britain was shown the supremacy (dominance) of money capital over industrial capital. Here is another proof of this: after the war of France and Spain in 1823 the independence was recognised of the states of South and Central America, being earlier Spanish and Portuguese colonies, and together with this a major flow of British capital occurs; from the above-mentioned numbers of British loans for 1821–25 half was directed to these states; and the point is – these loans, as the primary factor, called forth an increase of export of British commodities to these countries, as the secondary factor; in the fourth year the export of British commodities to Central and South America grew more than double, 'in fact the payment (of loans) was carried out not by precious metals or, at least, not by them alone, but in significant degree also by commodities',[681] the export of certain cotton fabrics to Central and South America grew from £1509 thousand in 1824 to £3596 thousand in 1825. In part due to this, the European countries guarded themselves from British imports by duties. As is known, speculation in Central and South America gave the impetus to the crisis of 1825. We likewise need to remark that also in time of the very war with France, loans and subsidies to British allies served as powerful stimulus of British export and produced in significant degree commodities; this is strongly emphasised by David Buchanan in his notes to Adam Smith. Such a state of affairs was preserved also in present times: very characteristic in this relation is the debate in British parliament in August 1923 apropos the loan for India of £65 million and the amendment introduced by sir Robert Hutchison [1873–1950] in the sense, to oblige India to spend 75% of its granted loan on purchases from Britain. In the words of the director of the Bank of England Palmer, cited by Tugan-Baranovsky, the first impetus toward the direction of British capital to Central and South America was given by the state [debt] conversions at the beginning of the 1820s. And indeed with all the speculative character of this feverish swoop to America, it carried all traits of imperialism, as export of capital... The

[680] Tugan-Baranovsky 1923, p. 38.
[681] Tugan-Baranovsky 1923, p. 42.

impetus to imperialist expansion, though it soon failed, was given by the conversions! Further: 'In 1824 and the beginning of 1825 – Tugan-Baranovsky cites from one of the directors of the Manchester Bank John Dyer – many Lancashire banks applied all possible efforts to expand their loans, and this led to the construction of new factories and setup of new manufacture in striking dimensions'. If these examples can be set aside as unhealthy signs of crisis, then here a converse example; at the end of 1825, in the depth of the crisis, when metallic cash in the Bank of England became less, than in 1797 and 70 banks suspended payments, the board of the Bank of England was already preparing again to suspend convertibility into gold, but the government decisively resisted this, and then the Bank tried the opposite policy: instead of reduction of its commitments it decided to expand them and came in this way to the rescue of the shocked commerce and industry of the country; and the point is – these measures were crowned with complete success, and despite the increase of loans, gold not only did not leave the bank cashboxes, but even flowed into it. These facts, getting in Tugan-Baranovsky a technical explanation, can be interpreted neither in the spirit of the omnipotence of the banks, nor of monetary *policy*, not in the sense of Keynes, but only as the supremacy of money capital over industrial capital. In this sense the comparison of both postwar periods, their currency ruin, must, in our view, give very meaningful results. The crises of the post-Napoleonic times were crises of the growth of British industry, the present crises – are crises of its decline. Then the supremacy of money capital was connected with imperialistic penetration in America, Central and South, today, as we will see below, it is connected with the reduction of foreign investment of British capital; today America, North [that is the United States], acts as a dangerous contender of Britain.

In the time of war with France the British banks catastrophically suffered; Withers informs that in 1793 there was a crash of over a hundred British provincial banks, and between 1810 and 1817 600 British banks closed;[682] in the time of the world war 1914–18 and after it there was observed in Britain nothing similar to that mass of crashes of banks – however those bank crashes were not so disastrous for money capital in Britain, as the currency ruin of our postwar period, Britain then did not face the threat of losing its championship on the world money market to the United States... As regards the situation of industry, then those clear facts of price fluctuations at the time of the big crisis of 1825, which Tugan-Baranovsky

[682]Nasse and others (1899), on the contrary, emphasise, that in the time of the wars banks extremely multiplied in the provinces due to the high conjuncture for the agricultural industry, and the crash of banks occurred after the wars due to the fall of prices in agricultural products. – This, apparently, speaks not in favour of the supremacy of money capital. Even if we do not interpret this contradiction dialectically, it, in any case, does not exclude the mentioned supremacy. Before us is a complex network of intertwining tendencies.

provides, were likewise by far not so murderous for British industry, as the present stagnation and unemployment; in general, the level of British commodity prices showed in the period of the war with France much more stability, than in the period of the world war and after it, it in 1821 returned to the numbers of 1788, whereas not so long ago Cassel in his memoranda for the League of Nations called the return to prewar prices utopian, about which also to dream is bad; the amplitude of price fluctuations was a hundred years ago insignificant in comparison with the galloping of the present postwar period; then the highest points (in 1801 and 1810) were 235 and 252 in relation to 135 (the number of 1788), while by the same standard the price level from 1914 to 1920 rose in Britain from 112 to 325, and in 1922 fell to 170 (number of 1900 = 100). Thus, on one side, we have now the much more difficult position of British industry; but, on the other side, despite of this, of paramount importance now is not so much the industrial, as the money power of Britain, [having] in mind the prospect of losing the supremacy on the world money market. With this, if in the period of Napoleonic wars the interdependence of interests of industrial and money capital in Britain was rather cooperation, than antagonism, then now there clearly looms precisely that antagonism, and the alternative: stabilise prices or stabilise the currency – laying at the basis of all present discussion and struggle of interests in Britain. On this we will still come to speak in the following, but for now let us note only, that, inter alia, the Napoleonic wars 1793–1815 cost (computed by Ernest Bogart[683]) 6 billion dollars, and the war of 1914–18 208 billion dollars, more precisely, if one subtracts the mutual credit of allies, 189 billion dollars; it is clear, that the world war had to affect far more serious consequences.

As precedent to the present situation of the British pound can be regarded also the history of the United States' restoration to convertibility into gold after the Civil War. The convertibility into gold was halted at the end of 1861 and resumed 1 January 1879: this was the period of the so called greenbacks (green notes), it was examined by Wesley C. Mitchell in his works: *A history of the Greenbacks* and *Gold, prices, and wages under the Greenback standard*. This precedent somewhat differs from the post-Napoleonic period in Britain and was not favourable for Ricardo and the quantity theory of money. Under an invariable quantity of greenbacks, the agio on gold fell from 45 to 23% after the battle of Gettysburg, Vicksburg and Port Hudson; on the other side, after the unsuccessful battle at Chikamauga the greenback fell 4%, and after the assassination of President Lincoln it fell 11% in one day;[684] the definitive triumph of the North gave a fall of commodity prices by 30% in a few

[683]Bogart 1921.
[684][Mitchell 1903, pp. 203, 204, 206.]

months, under the same quantity of greenbacks. The numbers of Mitchell show, by the way, the full parallelism between the movements of gold and commodity prices, wherewith the latter become general after two–three months. When it finally became known that at a certain date the convertibility into gold will be restored, the greenback began to rise in exchange rate and reached parity two weeks before this date. In Britain today the opposite happens: the government waits, evidently, until the pound reaches parity, and only then it will move to convertibility into gold.

2. Industrial and money capital in Britain

The Cunliffe Committee in 1919 with its work laid the basis of all post-war money policy of Britain. In general the committee determined the line of money policy of Britain on the side of deflation, though, to please industry, demanding 'cheap money', this in Britain is not openly admitted and one tries to arrive at deflation in practice with all possible caution, disguising it in every way. In fact even the 'labour' government in the person of its Minister of Finance Philip Snowden stood on the platform of deflation, considered it most important and urgent to raise the currency, state credit, to repay state debt, though this put a heavy tax burden on the population and increased unemployment. Below we will still return to the proposals of the Cunliffe Committee.

In the time of the world war Britain's state debt grew from £711 million (1 August 1914) to £8,079 million (31 December 1919) only in its consolidated part, while the current debt amounted to £1,349 million (31 December 1919). The circulation of banknotes rose from £29.7 million in July 1914 to 70.3 million at the end of the war and 132.9 million at the end of 1920. However Britain has not, like other states, proceeded on the path of further inflation and depreciation of its money. It already in the time of the war did more efforts in the sense of war financing not only by loans, like Germany and France, but also by extreme tax hikes. After the war its tax imposition exceeded four–five times the prewar one, income tax amounted to 4.5s. on the pound, almost 20% on average. Tax imposition per capita was estimated in Britain at £15 18s., in the United States £6 14s., in France £6 18s.[685] In the summer of 1923 Britain consolidated its war debt to America, pledging to pay each day in the

[685]These numbers are given by Lloyd George. The real, that is in products, and not in depreciated currency, tax imposition in Britain rose after the war approximately by two or two and a half times and constitutes 22% of the whole national debt against 11% in 1913 (see Heyer 1925). – Let us note that state taxes amounted in 1913/14 to £163 million, and in 1920/21 1032 million.

course of 62 years half a million dollars.[686] Almost half the consumable budget of Britain, roundly £350 million, goes to payment of the state debt. As a result on 31 December 1924, the consolidated debt of Britain amounted to £7,794 million, and the current debt to £845 million, despite the fact that debt to America (1 billion) would under consolidation of it be lowered by a per cent from 4.5 to 3.5, and, finally, let us note still the conversion of about £700 million of five and six per cent short-term bonds and treasury obligations into 3.5 and 4.5 per cent long-term loans.

This is very solid progress and repayment. But it is achieved at the cost of heavy casualties. Huge taxes lead to an increase in production costs of all branches, and this reduces British industry's chances on the world market, reduces its ability to compete with such cheaply producing countries as Germany. Improvement of the exchange rate of the pound was bought at the cost of extreme unemployment. A clear example of this we see in the interval from the end of 1920 to March 1922, when the exchange rate of the pound rose from 71.7% to 90% of its parity with the dollar, but then rose likewise unemployment from 1.6% to 16.39 of all organised workers, that is by ten times, and the number of total unemployed reached almost two million. Deflationary price movement – that was the conscious policy of 'money appreciation' – manifested first of all in lowering of wages. As a popular description of deflation can here serve the slogan 'offensive of capital'. From the end of 1920 to the beginning of 1922 the elementary subsistence minimum decreased in Britain from 280 to 170, but nevertheless, this was a time of severe social crisis. In 1921 British workers lost £6 million a week, in 1922 £4.2 million, in 1923 £4 million; the low price deflation harmed both industry and workers; the hope that it would facilitate British industry's competitiveness on the world market, did not at all materialise. *Nota bene*: low prices not in general, but low prices, as a result of deflation. The Midland Bank monthly review of July–August 1924 determinedly stipulates: 'It is a common place, that a decrease of the price level due to an increase of production is the best condition for the country's commerce and prosperity'.

All this showed the supremacy of the interests of money capital in Britain over the interests of industry.[687] If before the world war France was called the banker of the world and Britain

[686]It is understood, payment does not proceed daily, this estimation we give only for illustrative purposes.

[687]Withers 1909, pp. 166, 170, 171. 'It is often contended that the rapid expansion of German trade, which pushed itself largely by its elasticity and adaptability to the wishes of its customers, could never have been achieved if it had not been assisted by cheap credit furnished in London, by means of which German merchants ousted English manufactures with offers of long credit facilities to their foreign customers. ... [I]n considering the main springs which feed the flood of acceptance, we come to the London agencies of the chief Continental banks, which play a very important part both as sellers and buyers of bills'. – '[T]here is a strong feeling among the manufacturing classes that the facilities given by the London money market to foreign borrowers are detrimental to English trade. This contention cannot be set aside as lightly as it sometimes is by the defenders of our banking system. The obvious answer to it is that England makes profits out of its credit factory which very much more than compensate it for any handicap imposed on its manufactures of other (!) commodities.

was counter-posed to it, as the country of predominant industry, then this counter-position was lame; France was strong on the market of loans and investment, but on the bills of exchange, in general the purely-money market, London was the main centre of the world, it completely prevailed on the international market of gold. In the national economy of Britain a cardinal role was always played by such factors, as its position in international banking business, its income from foreign investment of its capital, from maritime freights, from its role of mediator in world trade, from its financing of world trade, from insurance and suchlike elements of 'invisible' exports. In the domain of industry Britain before the war definitely was outraced by Germany. This supremacy of money, money–commercial and commercial capital lies at the basis of all economic policy of Britain. For example: Britain more or less voluntarily and the only one of all the allies started to pay the war debt to America, since on the first place stand for it the interests of its credit, its prestige on the world money market; and, it is significant that, against the perspective of a deterioration of the exchange rate, the Baldwin agreement on the payment of war debt to America immediately raised the exchange rate of pound sterling – the calculation of Britain proved quite correct, because the exchange rate of the currency is primarily affected by the condition of state credit. Just as after the wars with Napoleon, Britain was first of all concerned with rehabilitation of its currency and conversion of its much increased state debt, – so Britain after the world war, too, does not spare efforts and sacrifices for the energetic repayment of its excessively increased state debt and for the restoration of the gold standard. Despite the fact that at present the money power of Britain has seen grow an extremely dangerous victorious rival in the shape of the United States and many are already inclined to bury Britain, as ruler of the money market, despite of this – and, perhaps precisely because of this, the interests of money capital and money power prevail in British politics now more than ever, forcing Britain to make feverish efforts in this direction. If previously, after the successful completion of the wars with France, the flowering of money power in Britain coincided with the higher flowering of its industry, then now, if one does not count the fleeting and illusory upsurge of British industry now after the world war, the interests of money and industrial capital of Britain commonly find each other more or less in conflict, sometimes even in sharp antagonism. Money capital was interested in 'dear money', in

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But it must be admitted that this is only a partial answer, and that if the handicap were real and persistent, its working would tend to make England a banking, discounting and exchange-dealing nation rather than a manufacturing nation; in other words, it would tend to turn our energies into financing, calculating, and book-keeping, rather than producing and working on commodities'. However Withers himself does not give a different answer, besides, that Britain must take as example this organisation of the foreigners, in order that '[t]here ought to be no possible ground for the assertion, that English traders cannot borrow in their own market as cheaply as foreigners'.

deflation, industrial capital was interested in 'cheap money', in inflation, of course, not in that runaway inflation, which took place in Germany and other countries, but in the 'moderate inflation' openly preached by the school of Cassel – one has only to recall the role of such inflation as an export premium.

Already in July 1923, when the pound also was close to parity with the dollar, British industry in the person of the Federation of British Industries vigorously protested against the government policy of deflation and the fall of prices and demanded a revision of the decisions of the Cunliffe Committee. Recently, in mid-March 1925, the same Federation sent the Chancellor of the Exchequer also a memorandum on the question of the return to the gold currency. With all the politeness of tone of this document, from it undoubtedly appears the counter-position of the interests of industrial and money capital in this question. The memorandum demands from the government that it as soon as possible will declare its intentions and put an end to uncertainty about the date of reform, 'so that it is possible to take one's measures for the immediate future, consistent with definitive knowledge of general money conditions'. But little of this; the memorandum of British industry claims that Britain's return to the gold standard is advisable only in the case if also other countries at the same time, too, will step on this path.

> At the moment industry most urgently needs stability in the national and international scale. It not can be achieved by actions of one side, but only by common agreement of the major trading nations about restoring the universal gold standard. If Britain acts separately, then the stability of the new standard will always be in danger, since we have not concluded with the central bank authorities in the United States an agreement on the regulation of the value of gold, for when the latter again goes down in international use. Such an agreement is absolutely necessary if we want to avoid big risks.

The memorandum demands that the resolution is taken into account of the currency commission of the Genoa conference, in particular on measures for the prevention of wide fluctuations in the purchasing power of gold and for more economical (!) use of it. But in the first place the representative of British industry 'insists in the most serious manner before His Majesty's Government on the earliest possible consultation' – of course, of industry. The president of the same Federation of British Industries points out that 'British industry suffers from the rising pound, an elevation, occurring in greater degree, than is justified by the comparative price level in pounds and gold; the high exchange rate of the pound,

naturally decreases the prices of British commodities in currencies of other countries'. On the other hand, Sir Robert Horn, speaking in Parliament, stressed that the appreciation of the pound is beneficial to Britain when importing foreign commodities. And, as is known, in Britain also before the war, import always exceeded export. Anyway, part of the British press particularly on behalf of industry speaks against 'financial purists' – bankers, in whose head hovers the restoration of the gold currency. So expressed itself, for example, *The New Statesman*.

The antinomy between money and industrial capital partly is observed also in the *Memorandum on currency 1913–22* of the League of Nations: 'In London and New York – it is said in this memorandum – clearing (current turnover) in much greater extent reflects the stock exchange, financial transactions and issuances of loans, than industrial dealings'. Similarly writes the London *Economist* (28 July 1923): 'At the present time with its large public debt and with high payment of taxes the demand for money for commodity turnover constitutes a smaller share of total demand, than before the war. This share is increasingly reducing, since prices fall faster, than debt is repaid'. We believe, that here is marked an important problem that science still will have to engage with in thorough manner. Partly in this problem can be seen the already known predominance of finance capital in our age of imperialism, the predominance of loans. We deliberately say of money (money–commercial) capital and do not use the expression: finance capital. This latter presupposes a certain connection with industry, whereas we note the discrepancy between the interests of money and industrial capital. Inasmuch as is it about the export of capital, the concepts of money- and finance capital come close to each other; however, also here they do not cover each other. Inasmuch as the power of the prewar position of Britain in the bills of exchange market, consisted of the fact that it 'received foreign money long-term, and lent them short-term',[688] it is clear that the loan (export) of money-capital on short-terms could not be identical with the imperialist penetration of finance capital into foreign countries. With this we do not at all want to say, that on the part of pre-war Britain there was no such penetration.

3. Gold as the basis of the pre-war position of Britain

The pre-war domination of Britain on the world money market had been closely associated with the role of gold as world money.

Before the war – says Withers – Paris, the Bank of France paid for its notes with gold or

[688]Keynes 1925a.

silver, at its discretion, 'so that anyone who has a credit in Paris has a credit which is of no international value, except in so far as he can make use of it, by means of the machinery of exchange, to buy a credit in London, which is convertible [into gold] as a matter of course'.[689]

> Practical financiers of all nationalities will admit that a draft on another centre is only valuable from the international point of view from the readiness with which it can be turned, through the machinery of exchange, into a draft on London, which is the real cash of international commerce and finance, because money in the real sense of the word, gold or its equivalent, is only to be had, always and without question, and to any amount, in London. (pp. 90–1) – But even though money (before the war) was not always cheaper in London than elsewhere (Paris), it was always more easily to be had. ... Paris often hands the borrower most of the money in the form of a draft on London. (p. 92) [A remarkable demonstration of the complete control of London over the world currencies appeared] in the autumn of 1907, when sudden crisis compelled the United States to [demand] payment in gold. Nearly all the gold shipped to New York at that time, estimated to have amounted to twenty-five million sterling, came from London. (p. 100) ... The unparallelled freedom and elasticity which mark the English system ... is found nowhere else. In New York bankers have to keep their compulsory 25 per cent of cash to liabilities, and the multiplication of credits, which create liabilities, is thus restricted by law. (pp. 93, 94) ... In London bankers' money merely means the right to draw a cheque, and is generally created by a banker lending it to a customer ... and the Bank of England can lend as freely as it pleases, for in its case its loans probably become its owns deposits, and the only restraint imposed upon it also is discretionary regard for the proportion between its cash and liabilities. – Nearly three-quarters of the deposits are created by loans and discounts. ... [Loans in one bank create deposits in another, and its deposits consist in considerable part of loans, made in other banks]: a delightfully simple system [of London], by which any one who borrows from it becomes its creditor. (p. 97)

And conversely: as stated by Stickney in his report to the American Bankers' Association in Milwaukee in 1901,

> England has so organized her capital by means of her magnificent banking system

[689]Withers 1909, p. 87.

> that she is the banker of the world, and with collects tribute from all the nations of the world in the form of interest, not for the use of her wealth or capital, but for the use of her credit. Paradoxical as it may sound, but it is literally true that by means of her splendid banking organization England collects interest upon millions and millions of her own indebtedness to other nations. It is a very profitable business to collect interest on what one owes, and it is this which makes England the creditor nation.[690]

In other words, London used the money of some of its clients for loans to others.

Here we came to the point having importance also for our time, marked by Keynes, that Britain received money long-term, and lent it short-term; below we still will see how in this respect contemporary America reasons. We note only that one of the main springs of British banking technique, a spring, expounded in detail by Withers, and in particular features by Edgar Jaffé (1905) is the institute of so called *bill brokers* (and the grown out of them discount houses[691]). Usually British banks act through brokers, namely providing them credit on demand or short-term (not more than a week), while the broker already has business with clients also with long-term loans.

Although Britain was before the war the prime country of creditors, its main banks, deposit banks, did not at all give long-term loans, as this would immobilise their received short-term money, yes they also did not have the apparatus for this.[692] This most important group of London banks refrained from promoter and issuance activity. These banks were conservative also in the sense, that they did not institute offices abroad; like also British industry, they waited that clients themselves would come to them. After the war this is changing, they founded so called *foreign banks*, with a network of branches in new and old light. It is characteristic, that this expansion met the greatest obstacles from the side of the government of the United States. – However, all this concerns only banks. The promoter business in Britain is mainly in the hands of so called *promoters*, professional–promoters and the stock exchange. But the banking apparatus of Britain before the war wielded predominantly short-term loans, that is money capital prevailed in it above finance capital. Long-term credit, of course, was also issued by the London exchange, but banks herein

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[690]Cited in Withers 1909, pp. 98–9.

[691]Later so called *stock brokers* and so called *merchant-bankers*, out of which grew accepting houses.
As regards accepting houses, then if, for example, a Brazilian planter sold his coffee, the buyer usually paid him by transfer to London (accepted there by the bank). Gold by this bill of exchange either remained at the banker for some interim period, or in general was given on the current account of the seller, but more often transferred from the current account of the buyer to the current account of the seller. So was created that reservoir, on which the London banks drew. Until their payment, bills of exchange ran also 6–8 months.

[692]Weber 1924 [see Nasse 1899].

played a secondary role.

Withers, as we have seen, is a zealous supporter of the theory, that money – is credit and, that 'banks make money'. As theory, it contradicts the apotheosis of gold in Withers, but facts live on. It is characteristic that the elasticity of London banks, which Withers so praises, now after the war, according to American bankers is not sufficient. They emphasise, that Britain has no bank notes, built on commercial paper, and therefore lacks the main element of elasticity, – due to restrictions, imposed by the Bank Act of Peel. It is also emphasised, that before the war the Bank of England was in close cooperation with the Bank of France, with its huge gold reserves and that now the situation, of course, is entirely different.

It is curious, that Withers, not allowing even a shadow of doubt on the 'dogma of gold', is forced to admit, that general opinion of the City considers the gold basis of British credit to be insufficient. However he brushes aside the unpleasant perspective by reasoning about the trust of the whole world in London, as money centre. A prophet is not without honour except in his own country – Withers, when he wrote his book, not only did not allow the thought that London may lose its dominant position; about American bankers, he speaks down condescendingly:

> It is a cherished ambition among Americans to see New York someday established as the monetary centre of the universe ... [but] the American is an excellent producer, a miraculous advertiser, an unapproachable gambler, and a somewhat questionable banker ... They have much to do and undo before they can constitute themselves into an international banking centre.[693]

Alas, the world war produced a revolution also here, it developed in America a system of 'federal reserve' banks, perfectly functioning. Equally little Withers knew about the impending 'revolution of gold'. He spoke on this point very 'strongly', for example: 'In fact, gold is the only commodity that is everywhere and always in the economically civilized world accepted in payment of a debt; and that readiness to meet liabilities in gold, at once and without question, is an essential part of a banker's business, as understood in this country'.[694]

4. The revolution of gold

[693]Withers 1909, pp. 88, 89, 90.
[694]Withers 1909, p. 266.

Let us now turn to the question about the revolution both in the actual role of gold, and in theories about gold, a revolution which appeared due to the world war. During the war gold depreciated in commodities by 60%. Then, from 1920, it again rises by 20%. Cassel and others determinedly speak about a fall of the value of gold (though Cassel denies in general the very category of value).[695] The Marxist professor Finn-Enotaevsky[696] rejects a fall of the value of gold, recognises however, a fall of its purchasing power in commodities; this last thing can be understood in the sense that not gold fell, but commodities rose due to the deterioration of production conditions during the war. Theoretically this interpretation is closer to Marx: the impetus was not given from the side of money, but from the side of commodities.[697] Cassel (in his *Memoranda* to the League of Nations on the money issue)

[695]His *The theory of social economy* raised part of bourgeois science on the board, as attempt to substantiate a political economy without the concept of value. But Gottl-Ottlilienfeld (1897) writes a whole book on 'emancipation from the term', on the 'dying theory of value' (*Abrechnung mit der sterbenden Wertlehre*) and so on. The prominent bourgeois economist Dietzel wrote a brochure (1921) [On the didactic value of the theory of value and on the basic error of the theory of distribution in Marx] and also tries to show in it, that 'the chapter on value can be dropped without any detriment'.

[696]See his 1924 work [translated article in this volume].

[697]We will not dwell here on the theoretical aspect of the concept of purchasing power of money, with which operates the latest bourgeois political economy; the reader is referred to the competent presentation of Finn-Enotaevsky in his book-anthology *Money and credit* (1925). Here let us only say, that today Cassel uses this concept for a replacement of the concept of value of the commodity, but it is nothing original or new, already a hundred years ago Bailey resorted to a similar expedient. Marx polemicises against the latter. '"Purchasing" – he says – means transforming money into commodities; money already presupposes value, consequently out with the expression "purchasing", otherwise we are explaining value by value; the term "purchasing" is unjustified and makes no sense without the concept of money' (Marx 1989b, pp. 327, 328). Marx rejects the concept of purchasing power as applied to the commodity, but he also does not apply it to money. In recent times came into use the definition, given in 1911 by Irving Fisher in his book: *The purchasing power of money*, namely: 'The purchasing power of money is the reciprocal of the level of prices; so that the study of the purchasing power of money is identical with the study of price levels'.

argues that where there is a change in the *general* price level of all commodities, the reason for this must lie not in commodities, but in money, here – in gold. For Cassel, the depreciation of gold occurred mainly due to the transition in war time of almost all the belligerent, as well as neutral countries, from gold to paper currency – this reduced demand for gold.[698] This explanation is accepted by many bourgeois economists. Of course, theoretically it badly fits with Marx's theory of value, according to which the change of the value of gold results from changes in the conditions of its production, the amount of labour spent on it; but Varga[699] stresses, that gold unlike all other commodities for centuries and even millennia is not consumed before wear, rather accumulates, and, therefore, the relatively tiny amount of annually produced gold cannot play a role – 'unlike all other commodities, Varga says, the price of gold in the modern epoch of capitalism is not determined by the cost of production of newly produced gold, but is a magnitude, historically fixed in a legislative order'.[700] From this it is not far to the figure £3 17s. 10.5d., which we met above and which a whole school of economists and politicians in Britain give a kind of 'mystical' significance, assuring, that gold currency that can only be restored in case, where the price of gold is again fixed on this apocalyptic number.

For our purposes it is sufficient to confine ourselves to empirical facts. And they in the most indisputable way speak of a depreciation of gold during the world war – whether this is a real drop of the value of gold or only a decrease of its purchasing power in commodities.[701] Moreover – contrary to theory (Ricardo argued that the value of gold as world money can not

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[698]Although gold import in the United States in the last eleven years amounted to about half a billion pounds, one should not conclude that the gold reserves of European banks of issue [that is central banks] declined; on the contrary, gold reserves in Europe have increased during this period by about half. At the beginning of 1914 they constituted £390 million in the 15 main countries of Europe, and by 1 January 1925 £560 million. In Germany, Austria, Italy and Russia they decreased, but in Britain they increased from £35 million to more than 150 million, in Spain they increased fivefold and now constitute £100 million, in the Netherlands they increased three to four fold, in Sweden more than two fold, in Norway and Switzerland more than three fold, in Denmark two and a half fold. How does the 'decline in demand' for gold reconcile with this? In the United States gold reserves increased from £400 to 900 million. During this entire period, the quantity of newly mined gold consisted of roughly £800 million. Since India and China, and also jewellery industry absorbed about £330,000, it is necessary to believe that the flow of gold into the United States was mainly due to new production, and not at the expense of the reserves of the world's central banks.
For 1924 world gold production amounted to £79 million (calculating an ounce of pure gold as 84s 11.75d), of this the British Empire produced £56 million, of which 40.8 million in the Transvaal. London exported altogether £49.4 million, of which about £30 million to the United States. Net gold import of the United States reached about £65 million. As one can see, the main import comes from Britain, wherewith the latter hardly holds for itself its mined gold: from its production of £56 million it exported £49.4 million.

[699]Varga 1925, p. 410.

[700]However, Marx himself speaks about the money markets, as about an exception from the rules of political economy. 'I really must investigate the relation between the rate of exchange and bullion. The role played by money as such in determining the bank rate and the money market is something striking and quite antagonistic to all laws of political economy' (Letter 23 April 1857 of Marx to Engels. Marx 1983, p. 126.).

[701][In the following Kapelusz has in mind the purchasing power of gold. It is distinct from the value of gold, see Finn-Enotaevsky 1927 in this volume.]

be different in different countries) – gold depreciated by no means the same in different countries. The largest gold depreciation we have in Sweden, where it retained in 1919 only about 20% of its prewar purchasing power; this is explained by the fact that in the time of war and starvation blockade, Germany inundated Sweden with its gold, Sweden was one of the few neutral countries, where Germany could buy products and so on – as a result the prices in Sweden terribly rose, this was a kind of 'gold inflation', there even was a ban of importation of gold, and instead of the pre-war slogan 'protection of gold' there was put forward, in the apt remark of Helfferich, the slogan 'protection from gold'. In France by 1918 gold kept only about 36% of its pre-war purchasing power; an extreme depreciation of gold in Britain took place in 1919–20, when it kept only 43%; in America in 1920 it kept only 44%. Germany stands somewhat apart, where depreciation of gold stopped in 1918 at around 65% of its pre-war purchasing power. So, we are witnessing here the presence of a 'revolution' of gold.[702] Even when in the fifties of the last century rich placer gold was discovered in Australia and California, and annual world gold production increased from 54,759 kilograms in the forties to 199,388 in the fifties (according to Soetbeer), the value of gold for the whole time up to the end of the sixties did not fall more than 30% (according to the index of commodity prices of Sauerbeck). But the catastrophe of world war immediately lowered gold in neutral Sweden by as much as 80%! According to the calculations of Lexis, world gold reserves grew from approximately 10 billion gold marks in 1850 to 52 billion in 1910, but the commodity price level (according to Sauerbeck) was in 1910 (after all the oscillations having taken place) the same as in 1850.[703] The growth of gold production kept pace with the growth of world commodity turnover. It is clear that the depreciation of gold during the world war could not have been caused by the growth of its mining. Instead of growth there was even a decrease. From 1920 onwards gold fairly quickly gains back about 20% of its prewar purchasing power, commodity prices correspondingly fall. This was a time of intense depression, world crisis; remarkably, here deterioration of trade conditions, if not purely industrial, then [certainly] sale conditions, manifested not in gold depreciation, that is more expensive commodities, but, on the contrary, in gold appreciation, as, for that matter, money usually under crises becomes more expensive. In this period, 1920–22, one can establish even some divergence of the movement of the level of commodity prices from the movement of the average market price of gold; the first came to be far behind the second. Faithful to his theory, Cassel explains the appreciation of gold first of all by the strong inflow of gold into the United States, which caused a demand for gold on the world market, and 'gold flowed to

[702]See Soldatov 1924 [*Revolution of the value of gold on the world market*].
[703]From 1873 to 1896 there was some fall of prices, and from 1896 to 1913 a rise of prices.

America because there it was cheaper to purchase commodities, that is the gold was there more expensive'. To this Finn-Enotaevsky objects, that wholesale commodity prices in gold ['gold prices'] were then in the United States considerably higher than gold prices of commodities in France, Italy, Germany and sometimes also Britain. Cassel himself does not confine himself to the above-mentioned explanation and tries (in the second *Memorandum*) to explain the elevation of the value of gold in 1921 as a 'conscious policy of deflation' in the United States, wherewith he attacks this policy, sees in it almost the main source of the world economic crisis.

We have traced briefly the actual fate of gold during the world war and the post-war period. What conclusions does bourgeois economic science draw from it in the person of the most active and prominent representative of it, Cassel, and his followers?

Cassel and Keynes throw gold from its pedestal, debunked it, declared it 'a barbarous relic'.[704] Cassel proceeds from the standpoint that gold lost now its main advantage, on which its significance previously rested, as world money and measure of value, namely the extraordinary stability of its value: the upheavals of the war and post-war time have not left even a trace of this stability, history passed it into the archive. Cassel argues, that, as a measure of value, gold now makes almost bigger jumps than paper currency. For proof he refers to the point, that in Britain with its paper pound commodity prices were exposed to far less volatility, than in the United States with its gold dollar. Recently (26 January 1925) Reginald McKenna, director of one of the five largest British banks (Midland Bank), gave to the meeting of its shareholders the following figures: in 1922 the average skewing of commodity prices from the annual level in Britain was 2.87, while in the United States 6.34, the corresponding figures in 1923 were 2.37 and 2.99, and in 1924, 2.58 and 2.91. (Keynes adds that precisely this comparative stability in commodity prices in Britain caused ('involved') the volatility of the exchange rate of the pound). The director of another big London bank (Barclays Bank) Goodenough cited in a meeting of its shareholders similar numbers. Cassel states that in our time the value of gold is no longer an objective magnitude, but depends on the value of the (paper) dollar, that is, on American bank policy.[705] This is exaggerated by *The New Statesman*: 'the value of gold depends on the whims of governments and central banks, exactly the same, as the value of paper money'.

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[704][Keynes with this referred specifically to the old gold standard in Britain.]

[705]Likewise says another prominent Swedish economist, Knut Wicksell (1922, p. vi): 'The since old times maintained naive belief in the value stability of gold, I think, now received a blow from which it will not easily recover. During and after the war this value of gold without any resistance, like soft wax, was subordinated to the evolution of means of credit, so that it could be rightly said, that the current value of gold is simply the value of the dollar, no more no less, or in other words, that it is completely regulated by the credit policy of the United States'.

In other words: going back to gold, Britain falls into even more dependence on the monetary and currency policy of the United States... 'A gold currency – says Cassel, – too, like paper, needs daily, hourly support and regulation by means of monetary policy'. This means in other words: the factor of monetary policy is stronger than gold itself, but the fact of the availability of large gold reserves makes the United States stronger than Britain in this domain of monetary policy.

Cassel translates his theoretical views on the role of gold not, however, into concrete proposals; in his report in the summer of 1924 in London he said, that 'despite the huge advantage of scientifically-regulated paper circulation, it is necessary to return to gold, and that another path has flatly not any chance in our time'. Only a few years ago in his *Memoranda* Cassel claimed, that Britain has a chance to return to gold, while it depreciated to 40%, but this will be almost impossible, if gold recovers a full 100%; now, when gold has gained back half (20%) of its lost value, Cassel suddenly came to believe in the possibility of the restoration of the gold standard.

Representatives of the banking world of Britain, the practitioners, do not agree with the recipe of 'managed currency', 'the influence of science on the element private capitalism' as Keynes preaches this (See his *A tract on monetary reform*, as well as his article in *The Nation* of 21 February: 'Individualist Capitalism in England has come to a point where it it can no longer depend on the momentum of simple expansion; and it must apply itself to the scientific task of improving the structure of its economic machine' [Keynes 1925a]). McKenna simply stated: 'As long as 90% of humanity finds gold currency the best, it is necessary for us to take this in account'. And one American banker was even more lapidary: 'All my life I considered, the more I have of gold, the better – how can I now throw all this overboard?' Sir Josiah Stamp, member of the directory of the Bank of England and former member of the Dawes Committee, responds to Keynes on behalf of the bankers as follows:

> We are against control of the currency by a central authority, because we cannot clearly see the technique and criteria of such, almost daily control of the currency, secondly – because we doubt whether the designated to this authority persons rise to the occasion, possess the technique, thirdly – because, it is necessary to believe, that the public will not have trust towards such controlled currency, in the public there is still spread even the prejudice, that gold currency means gold coin, fourthly – because in such central institution will be possible the influence of political parties (*The Times* even jokes, that 'as is known, politicians are bad economists') and, finally, fifthly –

> because management of currency will be complicated, in countries with big external trade and large capital investments abroad, by foreign exchange rates'.[706]

But, despite this rebuke, in the British debate on the benefits and risks of a return to gold currency both sides recognise[707] the instability of gold and extensively discuss, for example, such questions, of the kind, that after the return of Britain to gold there may occur a rise of the value of gold on a world scale, or, with an influx of American gold, on the contrary, a fall of it on the internal British market, a gold inflation.

Among the opponents of the proposed by Keynes 'managed currency' are Cassel (!), Edwin Kemmerer, T.E. Gregory and Edwin Cannan, and also Hawtrey, but because they themselves are supporters of the quantity theory of money, they are not in a position to move serious theoretical arguments against the reasoning of Keynes and so like the speaking on behalf of practitioners sir Josiah Stamp, highlight in their opposition mainly only the moment, that under currency management the government and banks can not completely become emancipated from political influences. We are here not going to dwell on the by Marx refuted quantity theory of money, known already to Locke, more developed by Hume, Ricardo, and James Mill, and in our time improved by Irving Fisher. Already in 1832 Tooke in his testimony before the parliamentary committee said: 'In the research I have had occasion to make ... [I found that] the rise of prices has preceded any large issue of Bank of England paper, and a fall of prices has preceded a contraction [and, therefore, cannot be the result of them]'.[708] As a striking concrete refutation of the quantity theory can serve the fall of prices by 44% in the United States in 1920–21 happening under an unquestionable and very extensive increase of the money mass.[709] The main idea of 'managed currency' of Keynes is that it would be possible to achieve internal stability of commodity prices at the expense of external exchange rate stability. This opposition itself is typical, it reflects already repeatedly the by us underlined contradiction of industrial and money capital interests in Britain, in this regard the views of Keynes represent undoubtedly symptomatic interest, but in essence

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[706]The journal *The Round Table* writes: 'While we have been fortunate to have had sound financial guidance during the last few years, we do not regard that experience as an adequate test of a “managed currency”' (1925, 15, No. 58, 'The gold standard', p. 252).

[707]The same Sir Josiah Stamp at the end of March 1925 states, that 'the gold standard proved during the period from 1874 to 1914, that it is the most capricious of all of our social tools and regulators'; Stamp accuses it no more nor less in the sense, that it does not instantly and automatically adapt wages to the changed price level, and in the April issue of *The Observer* Stamp puts forward the proposal to form an Anglo-American banking syndicate of owners of gold mines, that by sales of gold or holding it in 'warehouses' shall regulate the free gold market.

[708][Secret committee on Bank of England charter 1832, p. 289.]

[709]Let us also point out that the assignats of the French Revolution depreciated not due to excessive issuance of them, but, on the contrary, their depreciation forced the resort to new growing issuances. See Fal'kner 1919. The same was the case with our sovznaks.

they do not stand up to scrutiny. Keynes proposes, that the central bank institution in the country would buy and sell gold on by itself set prices at regular definitive intervals and thus affect the external exchange rate of its inconvertible paper currency; for example, sending gold into a country with the 'archaic' gold standard, Britain could raise commodity prices in the latter and so – this is the postulate of the theory of purchasing power parity of money – improve the exchange rate of its currency. Although Britain is itself the largest producer of gold in the world, these proposals are completely utopian.

To Keynes objects Anderson, 'economist at Chase National Bank of the City of New York', as he himself calls himself. When – he says – commodity prices increase not due to the growth of real value commodities, but as a result of a fall in the value of money and the exchange rate of the currency, then instead of an increase of production (which would happen under the gold standard) or savings there will take place, on the contrary, speculation; people, in expectation, that their money will fall even more, will only spend even more of it. Under the gold standard an unfavourable balance of trade and a poor currency exchange rate helps reduce import and expand export; but once the gold standard is replaced by an inconvertible currency, there occurs the opposite – importers try to bring as much as possible, before the currency will fall even more, and so on. If Keynes's plan would be realised, it will render the country to the sacrifice of speculation, which, studying the movement of price indices in various countries, will try to anticipate in its favour the government alterations of the exchange rates and its speculation will even more contribute to the volatility of these rates.

Even more sharply, than Cassel, professor–banker Irving Fisher in America attacks gold. He appeared before a special committee of the House of Representatives on the question of the possibility of combating the flow of gold to the United States: 'We are on the edge of a precipice' – that is the main tone of his expertise. 'A large stock of gold is a heavy threat to the entire economic life of the country'. Irving Fisher also points out that from the time of the concluded armistice the United States already experienced two periods of unstable prices, and that this was very costly to the country: in 1918 in circulation there was launched a lot of liquid money, and as a result the cost of living rose by two and a half times against the prewar [level], and in 1920 the central bank fell in the opposite extreme, in deflation; its results was the impoverishment of hundreds of thousands of farmers and merchants and a huge army of the unemployed. Fisher proposes his project of dollar stabilisation: every two month, the government should establish the value of the dollar on the basis of the index number of the 75–125 main commodities, gold is withdrawn from circulation and replaced by certificates for a certain amount of gold, standing in direct proportion to the movement of the

commodity index. These technical measures should 'deceive' the real movement of capitalist conjuncture (see his book: *Stabilizing the dollar*). Irving Fisher refers to Keynes, [for the point] that the gigantic gold stock of the United States brought it a loss annually of $420 million of potential interest, if gold did not vainly lie in banks. To avoid price increases and not appreciate with this its dollar, the United States (until recent times) followed the policy of 'sterilising' the gold coming to it, hiding it in the cellars of its banks. 'In the end, – says Keynes, – to protect the value of gold by artificial means, it would be much cheaper for the United States to buy up the South African mines in order to close them down, rather than buy up their output year by year in order to bury it'.[710] It is a mistake to think that the United States did not pay for the flow of gold to it; payment of British debt began only recently. Keynes argues even that America gives its products for the gold for nothing; it is afraid to raise its commodity prices, to not thereby devalue the dollar. Keynes goes even further and argues that even by loaning abroad America will not be able to sell and reduce its 'golden burden': if – he says – loans always meant a drain of gold abroad, then they would have been possible only for gold-producing countries.

The above given, undoubtedly, is not free from one-sidedness and exaggeration. By the way, the British supporters of gold respond to Keynes, that the so abused instability in our time of the value of gold in fact is not a drawback, but a merit of gold currency, indicating its elasticity, that it quickly adapts itself even to all perturbations and turbulent vicissitudes of the post-war period. It was also in that sense, that fluctuations in commodity prices are a main spring of the modern economy, this – is the bread for capitalism, without it the latter cannot live.

5. The Dawes Plan and 'currency imperialism'

Let us now turn to the events of the latest times. No matter how tempting it would be for Britain in terms of its rivalry with the United States to finally abandon gold and become the head of all countries with weak currency, entering by itself the kind of by Keynes preached artificial currency and make the countries with soft currencies into its currency vassals, no

[710][Paraphrased from Keynes 1924 (1981, p. 176).]

matter how tempting the prospect would be to leave America 'sit on its bags with gold' (Bendixen), the real facts prove stronger. The rivalry of America forces Britain to try as soon as possible to win back its lost position in the world market of gold and restore its gold currency.[711] On the other hand, also the United States is forced to withdraw from its abnormal situation of miserly knight, risking 'suffocation' in piles of its gold. The United States had to meet Britain. The United States sees the risk of the 'shining isolation' of its currency, it is interested in moving Britain and after it other countries to gold currency, so that gold again becomes world money. In this spirit determinedly spoke the Commission of Gold and Silver Inquiry and the formed under its representative John Parke Young sub-commission *European Currency and Finance*, collecting material for proposals of the congress.[712] Very significant and characteristic was the report of the Federal Advisory Council to the governors of the Federal Reserve banks of the United States in May 1924.

> The council urges the Federal Reserve Board to examine very closely into the powers vested in this respect in the Federal reserve banks and to study the question how far it may be desirable to amend existing rulings and regulations in order to approach the problem of Europe's financial and economic reconstruction in the most helpful spirit, in the same manner as is being done by the Bank of England and other central note-issuing banks.
>
> Unless America finds ways and means to permit her excessive banking strength to benefit other countries, particularly those striving to bring their house in order, the dollar cannot maintain its position as a world standard of exchange, and foreign countries—and even American banking and commerce—will, once more, in a larger degree become dependent upon and tributary to the pound sterling, to the greater exclusion of the dollar. It is idle, however, to preach the use of the dollar unless at the same time we render it possible for other countries to avail themselves of our dollar facilities. It is obvious that our credit power[713] cannot continue to grow indefinitely without the danger of over-saturation. If the stream of gold that floods our shore is not stemmed in time it is to be feared that ultimately we will not be able to ward off its inflationary effects. ... But ... the problem ought to be weighed from another and even

[711]The British Empire is the largest producer of gold in the world. Some see this as an incentive also for Britain to return to the gold standard.
[712]When these lines are written, we read in the newspapers the following telegram from Washington (10 March 1925): 'The Commission of the Senate with the following takes official steps for the convocation in Washington of an international conference with the goal of an agreement on the return of all currencies of the world to a gold basis and, thus, on the uniform stabilisation of them'.
[713][Kapelusz translated this into Russian as 'our gold reserve'.]

> more important angle. It is the question of whether, the world is more likely to regain the blessings of economic stability under the sway of several fluctuating standards of exchange or by a general return, as speedy as circumstances may permit, to definite relations of exchanges to gold as the ultimate measure and regulator.
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> The Dawes report leads the world to the cross-roads in this regard. It provides for a German note-issuing bank on a gold basis, but leaves the door open to place it on a sterling basis, and it cannot be denied that there is no small probability of the latter basis being chosen. In the opinion of the council the sooner Germany can be placed on a gold or gold-exchange basis the sooner can England, and other countries also, return to an unrestricted gold standard, while if Germany were placed on a sterling basis, England—in returning to an unrestricted gold basis—would have to pull not only her own weight, but that of Germany also. It is obvious, therefore, that, if the new German bank is placed on the sterling exchange basis, the world must prepare itself to remain on a basis of exchange instability for a prolonged period, the end of which cannot be foreseen, while the adoption of the gold (that is, the dollar) basis would accelerate the return to world-wide stability. ...
>
> The council recommends that, when the new German note-issuing bank provided in the Dawes plan is organized, the Federal Reserve banks take the steps necessary in order to facilitate the rediscounting in this country, of properly protected German gold bills...
>
> Measures of this character do not only tend to bring our gold hoard into active and healthy use, but, by enabling and encouraging other countries to trade in terms of dollars, we stimulate our own foreign commerce. We facilitate, furthermore, the direct sale in dollars of our own products, instead of making foreign countries and ourselves dependent in this respect upon Great Britain's acting as broker and banker, as naturally she would, where the pound sterling would govern as an exclusive basis of commerce and trade.[714]

This battle cry of the experts of the American central bank speaks very clearly. It is a matter, firstly, to prevent the United States 'being smothered' in its gold, and secondly, to maintain the dollar's hegemony on the world money market and in international trade, in the 'currency colonisation' of Germany and other countries. But here there is an important dialectical contradiction: America itself is interested in the transition of Britain onto a gold

[714] *Federal Reserve Bulletin*, June 1924, pp. 460–1.

basis, and therefore it is interested in the rise of the pound to parity with the dollar. The clothed and official language in the report of experts of the American central bank voiced that open secret, that the transition of Britain to a gold currency must increase the demand for gold and therefore is very desirable to America, fearful of depreciation of its gold reserves. The report tries to give its reasoning the appearance of care about, 'whether the world regains economic stability', but the egoistical 'devil's hoof' foully betrays itself. In the heat of battle for the gold discount bank of Germany the report agrees on the statement, that the transition of Germany to the gold basis of the dollar should facilitate and accelerate also the transition of Britain to a gold currency. Meanwhile it is clear, that the situation is quite the opposite: not impoverished Germany gives rich, still very rich, Britain a push in this direction, but, on the contrary, the victory in Britain of the gold currency will be, like fifty years ago, the signal for a whole number of other countries to return to gold. Recently, the president of the Netherlands Bank Vissering publicly expressed, that the Netherlands will wait for the initiative of Britain, although the Dutch guilder passed already over parity with the dollar. In the meantime, for America the most important was the following: while Britain remains under its paper currency, it is necessary to achieve the construction of a new German Bank not on the basis of the pound, but on the basis of the dollar.
For its part, also the British bankers sounded alarm. Walter Leaf, chairman of Westminster Bank, wrote in the June 1924 review of this bank:

> The possibility of combination between the dollar and a golden German mark, between the credit power of the United States and German enterprise in trade opens for us alarming perspectives, so long as the pound remains depreciated on the currency markets of the world. Between both two large gold currencies, the dollar and the mark, our depreciated pound would be forced out of the world of finance. For our self-defence then we willingly or unwillingly have to go to a gold basis, we will be forced to this. Is it not better, then, to make this step voluntarily, at the time that we ourselves choose?

Leaf proposes for this goal to raise the rate of the Bank of England to 5%, which should automatically lead the pound to gold parity. – Of course, the reasoning of the British Tit Titych,[715] fearing, that the German mark will ban the British pound, likewise badly hides, [that] the talk is about currency colonisation of Germany by British capital, about not

[715][Despotic merchant in Ostrovsky's play *Hangover at somebody else's feast* (1856).]

coming too late and not catching the place already occupied by America. About how the 'rehabilitation' of Austria into the League of Nations led to her colonisation by British banks, shrinking the local old Viennese banks, best of all testifies, [the fact] that in Austria now was introduced the *schilling* [shilling] *currency*; in the literal sense of the word *currency* colonisation![716]

If last summer, after the adoption of the Dawes Plan, the subject of dispute was Germany, then in January [1925] the question about return to gold is forced in Britain also by the examples of South Africa and Australia. The first decided to move to gold in February, the second suggests to do this in June [1925], and if before these dates Britain does not restore its gold currency, then there is a risk that both these important Dominions in currency relations come off of Britain and become vassals of the dollar. P. Maslov in the Comintern journal *Inprekor* even determinedly expressed, that the decision of South Africa shows the process of decomposition of the British Empire, motivated by the desire to break away from the metropolis. Australia too discloses attraction to America. However, as for South Africa, the experts Vissering and Kemmerer recommended to it to wait for the initiative of Britain.[717]

Returning to the report of experts of the American central bank. It was fraught with consequences and marks a turning point in the financial policy of the United States. Foreign investments of American capital made over the past year a jump uphill by three times: in 1923 $410 million, and in 1924 $1,263 million. American capital was placed in Europe in 1922 to the amount of $77 million, in 1923 of 93, in 1924 of $621 million. According to the British Board of Trade, the movement of capital from New York to London in 1924 was one hundred million pounds. From a comparison of these figures we can conclude that the lion's

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[716]The schilling currency was introduced in Austria on 1 March 1925. In the beginning was felt a complete lack of the respective coins and notes; therefore, the Ministry of Finance proposed to the National bank temporarily, until the demand is satisfied with enough amounts of silver schillings, to issue banknotes in 10,000 krone with a stamp on them stating: 'one schilling'; it will be made from early April; and the silver schillings are supposed to enter into circulation in late May. Also binding themselves in their currency to the pound sterling are Hungary, Danzig and Estonia.

Interesting and characteristic is the position of the currency in India. Here the British pound and the Indian rupee are mutually exchanged by governmental instances in fixed proportions. Twenty-five silver rupees were equated to one gold sovereign. This currency reform was carried out in 1893 and 1898. At the basis of this plan, of course, lay the considerations of British foreign trade with India. For 20 years India was an example of the so called *Gold-Exchange-Standard* (like in the Philippines), but in 1919 in connection with the postwar situation, according to Keynes's proposal, the exchange rate of the rupee was changed to gold. Now, the Swarajaya, nationalist party in India, seeks changes and on 27 January 1925 made against the government a proposal of the appointment of a currency commission with the chairman and the majority of members composed of Indians to study the situation. However, the Indian government itself announced on 22 January that it 'on the first place puts the internal purchasing power of the rupee, stability of prices, and only on the second place the external exchange rate of the rupee'. 'From 1893 to 1898 the supply of currency was a fixed quantity and the rate of exchange varied. ... Then the rate of exchange became fixed and the supply of currency variable' (Hawtrey 1919, p. 334.).

[717][Report on the resumption of gold payments by the Union of South Africa. Pretoria 1925. U.G., No. 12.]

share of American capital flowing into Europe chose its way through London. The age-old banking experience and connections of Britain in all corners of the globe contributes to it, that financial transactions of America also now went through London, using its banking organisation. This has raised the demand for the British currency. The flow of American capital into Europe raised, by the automatic law of the rate of exchange, the European currencies and in the first place the British, levelled off the unfavourable trade balances of European states. All economists – observers of the past year – converge in the opinion, that precisely the inflow of American capital was the main reason for the exceptional rise of the British currency in the second half of last year. In addition to improving the situation of the pound almost to parity, the autumn of 1924 saw the Swedish krona, Swiss franc and the Dutch gulden reach parity with the dollar.[718] It is very characteristic of the movement of the exchange rate of the pound, that it is mathematically almost identical with that of the flow of American capital into Europe: in January 1924 on the New York stock exchange for a pound was given only 4.21 to the dollar, in June 1924, 4.32, and at the end of January 1925 already 4.81 dollars. Of course, American capital came to Europe not for the beautiful eyes of Britain or Germany, it was primarily attracted by the usurious interests according to the Dawes Plan – we will in a moment acquaint also with another specific cause, the high interest rate in London, – but in any case, the own financial strength of America, its wealth of capital strengthened the position of its rival, Britain. This is the same dialectical contradiction, that we marked above. In this respect, Britain profusely and firstly squeezed the fruits in its favour of the adoption of the Dawes Plan. The question arises how much this enhanced flow of American capital in 1924 helped to release America from its 'golden burden'? Export of gold of the United States amounted in 1922 to $33.5 million, in 1923 – 33.3, and in 1924 – $16.7 million (counting a year from November to October). These figures are given by E. Schulze (*Neue Freie Presse*, 15 May 1925). However, according to the latest data, the United States from November 1924 to April 1925 exported $195 million, but imported 45, and in April the excess of gold export was 15 million, so one can not speak, like Schulze, about 'vain attempts of the United States to export gold'. Its plan consists not only in an effort to free itself from its gold, but also in preventing the fall of its value in the future. It is necessary to take into account also the inverse flux of European capital into the United States: in 1922 for $328 million, in 1923 for 394.

[718]This was facilitated by American loans to Switzerland ($30 million), to the Netherlands ($40 million).

6. 'Interest rate wars'

A high interest rate in Britain and a low one in America. Before the war such counter-position would have seemed incredible. Today this position of the interest rates shows the changed situation, the cheapness of gold in America. In modern theory of bourgeois economists the interest rate and discount rate plays a cardinal role both in the 'quantity theorists', and in the 'credit theorists'. To these rates is ascribed almost the role of super-natural panacea, with the help of which one can artificially regulate not only the currency, but together with it, all economic life of a country, to call forth at will that period of 'cheap money' and industrial boom, that period of 'dear money', compress credit and intentional depression of industry. '[It is] my belief that fluctuations of trade and employment are at the same time the greatest and the most remediable of the economic diseases of modern society, that they are mainly diseases of our credit and banking system, and that it will be easier to apply the remedies if we retain the control of our currency in our own hands'.[719] The erection of the interest rate as the prime factor of national economy shows, how one should not overstate the role and supremacy of money capital over industrial capital; here this is precisely an overstatement, first and foremost anti-Marxist, and we disassociate from it in the most decisive way. As likewise overstatement appears the theory of 'managed currency' of Keynes. But both of these exaggerations are symptomatic. In his big theoretical work Cassel tries to show that 'the low interest rate influences the whole market of capital in the sense, as if there occurred a real increase of available capital' and that 'a strengthening of available capital must sooner or later effect a corresponding demand and, consequently, increase production of real capital'.[720] And the rise of the interest rate lowers, according to Wicksell, the price level: the dearness of credit halts the sale of commodities. The world crisis of 1920–21 Cassel boils down (in his *Memoranda*), as to an original source, to the strong reduction of credit and circulation of notes of the American banks.[721] But it remains the question, whether or not this reduction of credit was not the cause, but the result of the crisis, whether it did not take place then when the fall of prices had already happened? Undoubtedly, the crisis had rather a commodity-, than money origin. Keynes, though also a supporter of this panacea of the discount rate, argues the diametrically opposite of Cassel:

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[719]Keynes 1925a.
[720]Cassel 1921b, pp. 379, 435.
[721][The Federal Reserve is often referred to in plural.] In his *Theory of the social economy* he in general sees in crisis only a phenomenon from the domain of credit, almost only a juridical fact of 'general inability to meet one's urgent debt obligations (Cassel 1921b, pp. 459 and 555). Capitalist overproduction he decisively rejects.

> The British and American central banks, – he says, – were guided by the correct principles, but carried them too slowly into life. They were slow in raising the discount rate, and then slow in lowering it. A lot of damage could have been avoided if the American bank and the Bank of England had raised the price of their money six months earlier and with the proper speed. On the other hand, to a large extent the unnecessary stagnation and unemployment could have been avoided, if in time was delivered cheap money. The governing authorities in Britain and America waited too long, until almost the culminating point of the conjuncture was reached, and only then they raised the bank interest rate up to 7%; and now (this was written in August 1921) they, apparently, again wait until conjuncture falls to the very minimum stage, and only then will decrease to 5% per cent. But if they, properly, had not the ambition to follow events, but to lead them, they would have already now decreased the discount as much as possible, at least until 5%.[722]

As we can see, the author of the idea of managed currency expresses himself here quite pessimistic about the actual management by banks of the crisis, and it is necessary to believe, that it was not just a lack of their 'ambition', but that crisis in general does not lend itself to be managed under the capitalist system. However, whereas Cassel sees the whole trouble in that banks stopped credit, and Keynes, on the contrary, finds, that banks did not direct events, but followed them, Lederer observes, that precisely American banks were able to take into account the market and dominate over it.

> When, – he writes, – in spring 1920, together with the fall of American prices the rate of exchange of the European drafts and consequently also the purchasing capacity of the European countries decreased, the larger organisations of American capitalism, the banks, decided to limit the credits in future and to demand the return of loans advanced; this was soon carried out on a large scale. ... Thus, the crisis spread to the whole domain of the world economy, in a time, when the whole world was still experiencing the greatest and most urgent need of American commodities.[723]

With this picture sketched by Lederer, Varga entirely solidarises, quoting the latter with the following commentary:

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[722]Keynes 1921.
[723]Lederer, *Wirtschaftliche Korrespondenz*, 7 February 1921.

> The advent of the crisis, – he says, – had been artificially accelerated by the large American capital. The concentration of property in trusts and the centralisation of the practical management of the enterprises has gone nowhere so far as in the United States. Therefore nowhere else can the market be so much under the direction of ruling capitalism as in the United States.[724]

Varga adds, that from the capitalist point of view such a limitation of credit was naturally most efficient (on 1 May the discount rate was raised to 7%), in that it averted a catastrophic overproduction.

However, these capitalist authorities themselves sceptically refer to such omnipotence of the discount rate, as a means to master the market. The London *Economist* recently pointed out that the increase in July 1923 of the bank rate caused contrary to theory not a fall, but a sensitive price increase; at the same time it also reduced unemployment, also counter to all theory. In the same *Economist* we read such reasoning: a high interest rate, should not to lower commodity prices, but, on the contrary, raise them, since the interest rate is a factor, going into production costs; therefore a high interest rate should promote not an increase of the pound, not increase its purchasing power on the domestic market, but the contrary. *The Economist* (of 21 March 1925) gives also very compelling numbers: for 63 surveyed joint-stock companies in various branches of production bank credit was only 11.5% of their paid up capital; therefore, 'an increase of bank interest by one per cent may affect joint-stock companies only in an amount, slightly greater than one tenth of one per cent of their paid up capital!' And meanwhile the average earnings of 312 companies, publishing their balance sheets for the last quarter of 1924, was 11.4%. In the face of these statistics those 'mystical' properties that Cassel attributes to a decrease in the rate seem completely incomprehensible: how one per cent can influence in the sense of increasing the production of real capital? Not less strange is the statement of Withers (from March 1925), that 'since the war, despite the strong increase in money circulation ... money was so inadequate in comparison with commodity turnover and funds, that the treasury and private market almost always have to borrow it from the banks, so that the bank rate constantly exerts its action'. In a new book Benjamin Beckhart, of Columbia University: *The discount policy of the federal reserve system*, the American author, despite his apology of the system of federal reserve banks, is forced to come to the conclusion that both the increase, and decrease of the discount rate occurred always with a lag, and that if even the rate increase can show a certain stopping

[724]Varga 1921.

[stalling] action, then the next following decrease of it is unable to neutralise already the result of the previous increase. To the same negative conclusion comes the American professor David Friday. Katzenelenbaum (1925b) notes that the Bank of France in the second half of the nineteenth century did not make the interest rate the object of its impact, while the Bank of England conducted this for more than half a century (from the 1850s–60s) but without success already at the very beginning, and all the more so even later; the discount rate ceased to be the regulator of the money market. This was explained by the fact that the role of issuance banks dropped significantly in comparison with the role of commercial credit banks. Plenge (1913) pointed out that in a climate of monopoly of cartels all the categories of banks already do not have the same possibilities to impact the money market. The policy of the Reichsbank and others now changed. Instead of a discount policy such banks, as 'Deutsche Bank' and 'Dresdner Bank', themselves distribute the quantity of loans to the connected with them enterprises. This stress Plenge and Katzenelenbaum. Reichsbank president Schachtm in a speech at the Congress of the Union of German industrialists, delivered in Cologne on 25 June, also stressed, that now in addition to the discount policy there is necessary the quantitative restriction of credit. So, the theory of the omnipotence of the interest and discount rate rests on very shaky foundations. However, like also in the matter of gold, here first of all the empirical facts interest us. But they eloquently speak in the sense that Britain and America in the last years hold battle with each other, carry a real war in the domain of the interest rate. If in the epoch of developed capitalism takes place the so called customs war, if in the epoch of imperialism the United States arranges in the republics of Central and South America military expeditions about the non-payment by these states of interest on loans deliberately imposed on them for this purpose of military–financial hegemony, then in the last years there appeared on the scene also another type of war, pure interest rate wars: here war is waged already not for interest [payments], but directly by these interest rates, here it is already not about guns beating out an interest, but the interest rate itself plays the role of gun... These 'interest rate wars' are a weapon of 'currency imperialism'.

When the pound already approached in the spring of 1923 very close to its pre-war parity and almost caught up with the dollar, American banks[725] raised their discount rate, with the result that the dollar rose and the pound fell; America then made a sacrifice, artificially introduced in itself 'expensive money' and a small slump, an industrial depression, only in order to lower the pound. This was a striking fact of the currency war of the pound and the

[725][Again, this probably refers to the Federal Reserve banks.]

dollar and it was carried out by means of the discount rate, a typical 'interest rate war'. Never mind, that in the new works on conjuncture of both the English [Cambridge], and the Harvard school the discount rate and the money market appear [as] the least sensitive indicators, responding only after prices and production. An 'interest rate war' is waged either on the domestic market (between different interest-groups), or on the external market. In April 1923 after the mentioned American manoeuvre, the London discount rate stood below the American and thus British capital began to flow into America; out of fear of this and the deriving from it falling pound the Bank of England in July 1923 raised its rate from 3 to 4%. At this height the official London rate remained until March 1925, while in America the abundance of free money capital forced [the Fed] during that time to repeatedly lower the rate, still in April it was reduced from 4.5 to 4%, and then lowered again to 3.5% in June 1924, and finally, even to 3%. Similarly decreased in New York the rate on commercial securities (bills of exchange) of various dates, and the loan rate occasionally fell to 2 and even 1.5%. In this was manifested the fact of the abundance of gold in America, the objective position, which, in the final light, compelled the United States to change anger into mercy and instead of an interest rate and currency war conclude with Britain a currency bloc. The low interest rate in America and the higher one in Britain led to it, that American capital streamed into Britain and increased in this way the exchange rate of the pound. We already have seen above the dialectical contradiction of this position. To it must be added that in Britain in that period market rates differed less from the official rate, than in America. Usually the official rate in America is a quarter per cent below the market rates, and the official rate of the Bank of England a quarter per cent higher than the market rates. Partly returned also British capital, 'having fled from the pound' to America in the early Ministry of MacDonald out of fear of a tax on capital, and also the by Minister of Labour Montague-Barlow of the retiring Baldwin cabinet proclaimed inflation for the struggle with unemployment. Speculation partly played also a role: in the face of the vigorous rise of the pound and in anticipation of its further rise and restoration of the gold standard speculation bought pounds and with this 'hysteresis', in its turn, contributed to its rise.

However this idyll of the currency bloc of Britain and the United States was not destined to last, and soon it was replaced again by a war of the pound and the dollar on the chessboard of interest rates. On 25 February 1925 the official discount rate of the New York Federal Reserve Bank was increased from three to three and a half per cent. After this bank the other American banks had to follow. This increase by half a per cent produced in Britain the impression of an 'exploding bomb'. It meant that the United States had decided to impose a

curb on the flow of its capital to Britain, and threatened, that American capital would leave Britain, and the pound would fall. The exchange rate of the pound immediately after this increase of the New York rate fell from 4.76 to 4.745 and then to 4.61 dollars. The market rates in New York and London in the beginning of 1925 in fact almost equalised, and [now there] not merely threatened the cessation of the flow of American capital, but according to some signs, its reverse flow already started. To this joined still such circumstances, as the recovery of demand for money in the domestic American market, large purchases of gold in the United States by Australia and India, who offered for it pounds in the amount of some tens of millions and this contributed to the depreciation of the pound. And in this setting an emergency meeting of the Directors of the Bank of England (5 March) convenes, and imposes a decision about the raise of the rate from four at once to five per cent. The increase of the rate of the Bank of England always is considered in Britain an event of paramount importance, a kind of declaration of mobilisation (of the money market), but this time this move also altogether had the huge significance, as resumption of the currency war of the pound with the dollar. Whereas America upped the rate only half a per cent, Britain immediately raised hers by a per cent; this was motivated by the already mentioned divergence of half a per cent between the official and market rates. After the hike of the London rate the exchange rate of the pound immediately recovered and again went up to $4.78.

Both rate hikes, the American as well as the British, stayed admonishing, alarming symptoms; but the eruption anew of the currency war for now did not yet flare up further.

The question is: to what extent are all these moments transient and will the rise of the pound be again reduced to not, as it was in the spring of 1923, when, in the figurative expression of Lloyd George, the pound looked into the face of the dollar, in order to immediately turn back? The question is, whether the American credits to Europe are not a Trojan horse for Britain, whether in the final light, even after the restoration of gold currency in Britain (or even just because of this restoration), the winner will be only America? Is that assistance which America showed Britain in this domain not suspect? Who will be the final winner in the competition for the world money market? Is the present united front of the United States and Britain in the currency market durable or again to be replaced by a long war of the pound and the dollar?

There is no shortage of warning voices. The London *Economist* pointed out that 'the money flowing to us from the American purchases of European papers [securities], is only a temporary visitor', since from now on the flow of interest [payment] on these securities to

America must start, and, even more so, if there occurs a reverse outflow of the same capital. Cassel warned (speech at a meeting of German bankers in Dresden 17 January 1925) that 'in Europe the dollar is valued now below its actual value due to the large American credits to Europe; this kind of rate of exchange is not a reliable basis for recovery of the gold parity of European currencies, this foundation could only be the real purchasing power parity'.

With regard to the momentous meeting of the governor of the Bank of England, Sir Montagu Norman, with the chairman of the American federal reserve, Benjamin Strong (this meeting took place at the beginning of the present year and it was in connection with the transition of Britain to gold currency, proclaimed by Winston Churchill), the American press wrote very pointedly, that the United States cannot take on itself the obligation to keep its rate at its present low level going forward; so wrote, incidentally, *The Journal of Commerce*, a good informer. With all the friendly tone of the American press, it emphasised, however, just like in Europe the editorial of the German journal *Bank*, of Alfred Lansburgh, that Britain, seeking to restore its gold currency, tries to do this not organically, not by own efforts, not by a price decrease wrestle with inflation, but exclusively in the hope on American help, which must give her the opportunity to get round without victims, connected with deflation. But in Britain the conviction is strong, that insofar as she builds her hope on the credit policy of America, she even in much greater degree than before gives herself into the arms of America. *The Statist*, dwelling on the danger, that the return of Britain to the gold standard places the financial and credit policy of Britain under the control and dictate of America, since the latter is master of more than half the world's gold reserves, soothes the reader by the indication that over the last years the pound in any case always was dependent on the dollar, every change in the commodity price level in Britain (that is the purchasing power of the pound), as well as in other countries, took its start in America, but now, with the introduction in Britain of the gold standard, 'this formerly unstable correspondence of the dollar and the pound will have to be replaced by their cooperation–competition (*close concurrence*), wherewith Britain will have to get an incontestable right of say in the policy determining the value of gold'. This reasoning is little convincing. Already not to speak about the contradictory term, which we translated in the sense of cooperation–competition, America is interested in enforcing the value of gold, and for Britain this will be a disastrous prospect, will entail a fall of prices and the all distressing deflation and industrial depression.

Keynes claims, that the gold standard, formerly useful to Britain during the time of its money omnipotence, now, when the latter transferred to America, is not beneficial to Britain and makes her even more dependent on America. Exactly likewise opponents of the restoration

of greenback convertibility into gold argued, that this convertibility would make America 'hewers of wood and drawers of water' for foreigners. The point being, that the America of that time was a debtor abroad, wherewith its debts were often denominated in greenbacks: of course, an increase of the latter to parity with gold meant a real increase in debt. But in present Britain the situation in this regard is otherwise: its debt to the United States in any case is denominated in gold, and since Britain is still in relation to other countries a creditor country, its loans to them are denominated to them in pounds, just as the majority of its investments abroad, and therefore the elevation of the pound to parity with gold can be only beneficial for Britain.

As a historical reference, not holding, however, any analogy, we will inform here, that the first French Republic, too, desired to have its coin, independent of foreigners. On 26 floréal of year III [15 May 1795] Jeanbon Saint-André delivers in the Convention a speech, [proposing new decrees] on the legal tender of assignats:

> Gold and silver, – he says, – are the fruit of a foreign world, today hostile to us. ... They form the monetary system of the enemies of the revolution, cosmopolitans ... But you, the lawgivers, who want to found the French liberty, ... organise your social system independently from the rest of the world.[726]

It is curious, that also Jaurès shares the opinion of the then leaders, that the depreciation of the assignats was influenced, mainly, by foreigners.[727]

7. Currency imperialism and finance imperialism

Pessimists predict that the slightest increase of the bank rate in the United States again will force Britain to go the same road and take 'heroic measures' for the retention of its gold in the country. But this struggle on the basis of interest rate has another, very important side, because it cannot help but touch the question about capital investments abroad, the question about the imperialism of finance capital.

The British government, for the sake of the exchange rate of the pound, put pressure on the big London banks in the sense, that they should abstain from conducting foreign issuance, loans to others countries, since the outflow of British capital would harmfully affect the

[726][Saint-André 1795, pp. 4–6. The essential ideas of the lecture came from Caffarelli du Falga.]
[727]Jaurès 1901, pp. 1025 and others.

pound; Churchill was effusive apropos this in praise of the discipline of British financiers and large banks.[728] But this is a double-edged sword and also has its downside for Britain, as the countries, seeking a loan, are ever more turning to America, and the latter makes its customers even of British Dominions, like Ireland and Australia. Although the actual American credit to European countries costs not at all cheap (generally not less than 7.5%), it is still cheaper than British, especially, if Britain for confinement to itself of its gold under the gold standard will have to raise its rate even further. In this way, here the interests of the pound, currency, come into direct clash with the interests of Britain in the domain of the world fund market, the market of loans. This – is the most dangerous contradiction. Here along with water, as the Germans say, splashes out of the bath the baby itself, once Britain restores its currency [at] the price of a rejection of imperialist penetration of its capital in foreign countries. In this antinomy can be seen the contradiction of the interests of money–commercial and finance capital, 'currency'- and 'financial–industrial' imperialism, the contradiction which we pointed out at the outset. If, as we have seen above, America with its export of capital is playing into the hands of the British pound, then here we see as if the opposite pole of this dialectical contradiction: the restoration of the pound, requiring a compression of British investment, plays into the hands of America on the international loan market.

This contradiction between currency and loans does not hesitate to recognise, as something completely normal, the already quoted by us Anderson: 'it is profitable to borrow in terms of a money which is expected to depreciate'.[729] In other words: who loses on depreciation of his currency, on the other hand increases the range of his customers in the international market of loans, expanding the imperialist scope of his finance capital. But the argument of the American economist is much more interesting and symptomatic in another relation, clearly illuminating the prospects. London, – he says – undoubtedly can secure for itself its old hegemony, as world money centre, insofar as this means hegemony in the financing of maritime shipment of commodities from one corner of the world to the other, and likewise short-term bank and currency transactions; as for New York, then in all likelihood it will remain for a long time the main world market of capital, insofar as this market differs from the money market, it is the main market of international long-term loans. As we can see, these prospects touch our problem of money- and finance capital. In the same spirit speaks a dispatch from America, placed in *The Times* of 22 January 1925:

[728]The abstention from investment replaces by itself elevation of the bank rate.
[729]Anderson 1925, p. 13.

> In general the banking world of America discusses the problem of the restoration of the gold standard in Britain in the following way. To keep the pound at parity, Britain will have to abandon its old predominance, as market of long-term foreign loans, and orient the discount policy of the Bank of England to the maintenance of the role for London of market of short-term loans, namely on the basis of a higher interest rate, than in New York.

In these words, is shown, perhaps not so much the actual position, as the intentions and hopes of the United States. We shall see below that this is somewhat contradicted by the tendency of post-war Britain to predominance of long-term (mainly public) loans. On the other hand, in contemporary America is manifested the tendency to 'industrialise' investments: while Britain increasingly puts its money into state-, coupon loans, America is trying to put its foreign investments in the private hands of Krupp, Thyssen, and so on, rather, than in the hands of the German government, and in Germany this goes even to the attempt to create its type of 'bond–share', a synthesis of coupon and dividend security.
Note further, that since the world war the United States are beginning to compete with Britain also in short-term acceptance credit, constituting the pre-war strength of Britain in the money market.

> To the system of the united reserve banks belongs also that merit, that they have taken a significant part in the dissemination in the United States of bills of exchange – acceptances, which before had here almost no roots. Now there arose a lot of rich capital companies to finance and facilitate foreign trade. Therefore, we can speak here of conscious and systematic effort to increasingly replace bills of exchange denominated in sterling by American acceptances.[730]

Rivalry on the ground of currency imperialism, the rivalry of the pound and the dollar, is closely connected here with trade and export itself.
However, the British themselves recognise the shift accomplished after the war in the world capital market. The British newspaper *Financial News* (13 May 1925) writes in full accordance with the American Anderson: 'New York now occupies first place in the world capital market, insofar as it is a matter of long-term credits; it is not expected that this could change in the near future. But we do not see grounds, that Britain would leave its leading role on the short-term credit market [that is the money market]'.

[730]Hasenkampf 1924.

Apparently, everything speaks in favour of such a change of things. We here only would like to emphasise that the leading role on the short-term loan market is not be underestimated, calling it the role of 'top, global money-changers, earning on transfers, on commission and so on' – as one Russian author recently expressed.[731] We have seen above, what a pre-eminent role played precisely short-term loans in the pre-war money power of Britain, at least in its banking mechanism. And if now, as emphasises the same author, the restoration of gold currency in Britain can help her only on the market of short-term loans, where 'for the leading role it is not even necessary to have a significant amount of own capital, since while London sends one amount, at the same time, it gets another'; if, on the other hand, the restoration of the pound can not replace and change the fact that America is much richer after the war than Britain in capital and therefore much stronger than it in the domain of loans (long-term), – then this does not yet predetermine the question about the specific weight of 'currency'- and finance imperialism, about their relative importance. It also does not solve the problem: in how much the role of 'top, global money-changer' contributed to the former power of Britain also on the world capital market. This is partly the same antinomy between money- and industrial capital. And in any case, even if Britain now lost its former supremacy, this will only exacerbate the contradiction between them. As we mentioned already above, instead of the cooperation of the post-Napoleonic era now there is antagonism.

Contemporary Britain, although its pre-war investment of capital abroad reached the very impressive figure of $18-20 billion (of which in the first half of the war Britain has sold 5 billion and by the end of 1923 its foreign invested capital amounted to $17 billion; see Fisk 1924), significantly is behind America, especially outside the European countries. The amount of foreign investment of the London exchange for 1924 amounted (according to *The Statist* of 28 February 1925) to £135.4 million; this reaches 62% of foreign investments of the New York exchange during the same year, or 41.5% of foreign investments of the London exchange in 1913 (the latter figure *The Statist* gives as £197.5 million, but in terms of current prices it should be £325.9 million).

With regard to the total amount of private foreign investments of America, it has increased them from the pre-war time until now from $2.6 to 9.5 billion, and together with the military state loans of $11.5 billion this now is $21 billion (figures of Schulze-Gaevernitz). Let us report still, that foreign investments of France amounted on the eve of the war to $8.5

[731]"Perspektivy ekonomicheskogo razvitija Anglii v svjazi s perechodom ee k zolotoj valjute' [Prospects of economic development of Britain in connection with its transition to gold currency], in the collection *Za rabotoj*, Mosk. Rabochij, May-June 1925.

billion, but at the end of 1923, taking into account its sales and loss on Russia, $5 billion, while the investments of Germany before the war [amounted] to $5–6.6 billion, and at the end of 1923 1.6 (Fisk). Further: in fact, despite Churchill's praise, Britain in the last year invested much more money, than her possibilities of its balance of payments allow. In this regard the following recently published statistics of the [British] *Board of Trade Journal*, 1-2 in 1925 (in million £) are revealing.

	1907	1913	1922	1923	1924
Surplus import	142	158	171	203	341
Net income from maritime freight	85	94	110	115	130
From foreign investment	160	210	175	150	185
Remainder	35	35	40	40	55
Income from all invisible export	280	339	325	305	370
Active balance of payment	138	181	154	102	29
Foreign investment	91	198	135	136	134

As one can see, the activeness of the balance of payments in comparison with the prewar time decreased from £181 to 29 million, but foreign investment only from 198 to 134, wherewith for the last single year was there occurred a colossal deterioration of the balance of payments from 102 to 29 million. The question is, from where Britain took this sum for foreign investment? Unless Keynes is right and Britain put abroad long-term, that, which it received short-term from the inflow of American capital.[732]

Proponents of the gold standard emphasise, that under its automatic regulation, so called *overlending* is impossible, [whereas] excessive lending abroad, is possible under inconvertible paper currency and artificial discount rates. American authors (Anderson)

[732]This – is one of the bases of the pessimism of Keynes. The situation of Britain on the world money market, he says, is the diametrical opposite of the prewar, when Britain, by contrast, received foreign money in general long-term, and lent it short-term.

explain the fact of such abnormal excess lending on the part of Britain by its 'artificially low interest rate'. Of course, from the point of view of hegemony on the international loan market a reduction of British loans abroad is advantageous to imperialist America. However, also in Britain not only Keynes, but, for example, the director of Lloyds Bank Henry Bell, a supporter of the return to the gold standard, declares in *The Times*: 'Perhaps it would not be bad to give foreign loans a rest'. We have seen: this was not the business of banks. But Joseph Kenworthy in the article 'A ban on loans' (*Daily Mail* 15 June) wrote, that it is time for Britain to regain its former position on the world money market, where now America exclusively prevails; for this it is necessary to establish financing and lending not only to the Dominions and large foreign companies, but also to foreign governments on the Continent.

In 1924 the total amount of private [credit] issuance in the United States reached $6.3 billion, and by six times exceeded the British.

Even more characteristic for judgement about the role of foreign investment of Britain in the pre-war and post-war time and for its comparison in this respect to contemporary America are the statistics of the American journal *Investment Review* (cited from the London *Economist* 24 March 1925) in which are listed similar figures about France and the United States.

(In millions of dollars)

	Britain		France		United States	
	Total sum of issuance (without treasury and so called *refunding issues*)	Foreign investment in % of total sum	Total sum of issuance	Foreign investment in %	Total sum of issuance (without state and municipal)	Foreign investment in %
Average 1911–13	998.6	82.2	1089.9	78.1	–	–
1920	1345.2	10,7	961.5	0.9	2963.1	9,8
1921	1497.6	29.0	1221.3	0.6	2377.3	18,8
1922	2518.4	22,6	1403.0	0.1	3242.5	19,7
1923	1234.8	50.6	843.5	6,5	3289.6	7,5
Average	1649.0	26,3	1104.3	1,6	2968.1	13,7

1920–23						

From this table it is clear what feverish efforts Britain makes to win back its prewar position on the world capital market. The percentage of its foreign investments to the total amount of its issuance was before the war 82.2%, it falls in 1920 to 10.7%, but then rises in 1923 even to 50.6%, while it fell in France from the pre-war 78.1, even down to 0.1% and is not able to significantly rise. According to *The Economist* (14 February 1925), in 1924 the percentage of foreign and colonial[733] investment to the total amount of issuance of Britain was even about 64%: 134 million of 209.3 million – this denotes, that the government's efforts to tighten lending abroad did not yet have considerable success. From the other side, the table clearly shows us the danger of American rivalry in this area: on average in 1920–23 the absolute number of American foreign investment almost equals that of the British (America $406.6 million and Britain $433.6 million), and at the end of 1924 there was also altogether in this relation a turnover and record, American foreign investment almost twice exceeded the British.

Besides a quantitative shift, there was also a qualitative one in the composition itself of British issuances. We examined the change of the relation between internal and foreign issuances; before the war the latter strongly prevailed in Britain (82.2%), after the war they fell, and now are striving to make up the loss.

(in millions of pound sterling)

	Metropolis		Dominions and colonies		Abroad
	Private issuance	Public issuance	Private issuance	Public issuance	Private issuance
Average 1911–13	34,55	1,26	48,51	25,75	65,36
1922	68,33	375,9	9,52	65,6	33,89
1923	56,38	77,56	18,57	74,15	18,29
1924	60,56	24,05	16,07	56,21	9,41

This table shows us another qualitative shift: between public and private issuances, or, what is the same, between coupon and dividend securities. The above figures we take from the official German *Wirtschaft und Statistik* (27 February 1925).

In the post-war period in Britain there is observed a move of the centre of gravity from

[733]Wherewith colonial-, internal to the empire, investments get preference before foreign ones.

private-, dividend issuance that prevailed before the war, toward government and public loans, with a coupon. Private issuance in the metropolis, Dominions and colonies and abroad decreased from 145.42 million at the pre-war average to 86.04 million in 1924, while public issuance increased from 54.3 to 123.3. In the metropolis itself this reduction did not occur, but on the contrary, if one sets aside changes in the purchasing power of pound,[734] private issuance even increased from 34.55 to 60.56; but in the Dominions and colonies, we have a reduction of almost three times (16.07 against 45.51), and abroad even seven times (9.41 against 65.36).

In this qualitative shift, the decrease of private issuance precisely to abroad, is most profoundly manifested [the fact of] the alteration taken place during the war in the position of Britain, as the ruler of the world money market. The United States, the European continent and other countries became emancipated from the de facto monopoly of the London exchange. *The latter before the war was strong precisely in private issuances.* To what extent is possible also here the 'counter-position' between money–commercial and finance–industrial capital? To what extent can one establish the predominance of one or the other in private or public issuances? We have to confine ourselves to solely a formulation of these questions. Returning to concrete facts, let us note, that in the alteration of the centre of gravity from private to public issuances [there] were involved also other reasons, such as: disorder of the post-war economy and lack of trust, governments' need of money and so forth. But we can take one further step forward and establish a shift in these private issuances themselves in Britain, namely from one to other [types of] industries. In the numbers of *Wirtschaft und Statistik* the decrease after the war of issuance for railway construction is striking; before the war they constituted for Dominions and colonies 15.0% of the total figure of issuances, and for abroad 23.1%, but in 1923 only 1.3 and 5.9%; the absolute figures give an even stronger decrease from 21.83 and 33.45 million to 1.20 and 5.48 million. A great percentage increase, but together with it nearly stationary absolute figures can be observed for the following groups: factories from 6.6% (1913) to 12.5% (1924), wherewith 1920 and 1921 gave even 29%, then iron, steel, coal from 4.3% to 8.4%, electrical facilities from 5.2% to 11,2%, shipbuilding and ports from 2.6% to 7.2%.

8. Issuance and the gold reserve in Britain

[734]It is necessary to take into account this reservation for all figures. These statistics suffer also from the fact that in them direct purchases of foreign securities by American capital are not isolated from loans of new issuances.

In the question of the restoration in Britain of gold currency the discussion in reality was about the non-renewal of the ban of gold export. Pessimists feared the withdrawal of gold from the country. Even if the majority of countries retained their pre-war gold reserves in integrity and there is no basis to fear with Cassel an insufficiency of gold on the world scale (whereas Keynes insists, that there is more than enough gold, Cassel – in the already quoted speech in Dresden – predicts that the flow of gold into America will run out soon), the British nevertheless are extremely anxious that, if they carelessly lift the ban of export of gold (the date of the ban expiration is 31 December 1925), gold could leave them; they pointed out that the transition to a gold basis is dangerous, so long as the devaluation in France and other countries with a sick currency had not passed. Keynes, warning against a precocious lifting of the export ban of gold, demanded at least to wait a certain anticipatory period and make sure, that prices and exchange rates were established firmly and without oscillation. Although Keynes tirelessly stressed that a more 'scientific' standard is necessary than gold, Keynes is counted not so much to the theorists, as to the practitioners, but it is characteristic, that *The Times* (23 February 1925), objecting to Keynes, refers precisely to practice, which shows, that without risk nothing can be achieved. 'Experience warns us – it writes, – that if we will wait a more or less enduring time for the pound sterling to become at parity with the dollar and [that] the necessary fundamental adaptations will be taken, then we will wait indefinitely'. Here incidentally let us recall, that from the 2,000 gold bars, prepared for the transition of Britain to gold in 1821, only 13 were factually requested by the public: the same thing reoccurred in America under Treasury Secretary John Sherman, when after the Civil War metal currency was restored. Is there not here some vicious circle and does not the transition itself to gold create certain such conditions of its solidity, [which are] impossible without the fact of this transition? It is curious, that between Keynes and the Cunliffe Committee, proceeding from entirely different considerations, there is a congruence, the Cunliffe Committee also demands a certain anticipatory period.

> We recommend – says the Committee, – that the normal minimum of the central gold reserve to be aimed at should be, in the first instance, £150 million. Until this amount has been reached and maintained concurrently with a satisfactory foreign exchange position for at least a year, the policy of cautiously reducing the uncovered note issue should be followed. When reductions have been effected, the actual maximum fiduciary circulation in any year should become the legal maximum for the following year … . When the exchanges are working normally on the basis of a minimum reserve

> of £150 million, the position should again be reviewed in the light of the dimensions of the fiduciary issue as it then exists.[735]

If the pessimist Keynes, at the head of the opposition against the restoration of the gold standard, emphasises, that Britain has now six times less gold than the United States (the latter's gold is estimated at 4.5 billion dollars)[736] and that 'a movement of gold or of short credits between London and New York, which is only a ripple for them, will be an Atlantic roller for us',[737] then sir Felix Schuster, famous English financier, on the contrary, indicates that the gold reserves of the Bank of England even exceeded in 1924 the number of £150 millions (which the Cunliffe Committee thought sufficient for the passage of the reform), and insists, that Britain boldly can go to the gold standard.

Let us present here some data on the Bank of England's situation (on 18 February 1925). In the Issue Department: gold in bars and coins – £128,579,230, other collateral – 8,734,000, government debt – 11,015,100; right to issue – £146,504,430 (Britain formally retained during the world war its old principle of *fixed line*, that each release over a certain number of banknotes should be completely covered). In the Banking Department: total amount of *currency notes* – £280,669,901, ensuring them banknotes £26,950,000 and £27,000,000 gold. The percentage cover amounted to 19.2% versus 14.4% four years ago, when the circulation of *currency notes* amounted to 333,674,380. On the eve of the war the percentage of cash (metal) to *all* liabilities of the bank stood at 52.40%, and the gold reserve at £40.2 million. Circulation of banknotes amounted on the eve of the war (July 1914) to £29.3 million, and now (18 February 1925) £124,200,000 million.

Thus, the circulation of money in Britain still consists of 400 million pounds. This is a lot bigger than the pre-war figure, an undoubted inflation. However, in addition to the change in the purchasing power of the pound, that is aside from the high cost of commodities compared with the pre-war time, this figure cannot be directly compared with the pre-war figure of £29.3 million – by virtue of the development of turnover and so on. The actual excess of present money circulation in Britain over the pre-war stands at two – two and a half times. This approximately corresponds to the present situation of British commodity prices. That is why the increase of the pound almost to parity was not reflected at the beginning of this year onto British commodity prices, that is on the domestic purchasing power of the pound. That is why, precisely so long as the quantity of paper money circulation is not

[735]Cunliffe Committee 1918.
[736]Per capita the United States had in the 1870s $3 gold, in 1913 $18–19, and in 1924 $40. In Europe at the end of 1923 there was only $2.2 billion gold.
[737]Keynes 1925a.

reduced, hopes for the restoration of gold currency in Britain are based on the expectation of foreign, American help, and most importantly – on a very widespread opinion in Britain, that the imminent gold inflation in America will call forth a fall of the dollar's value, that is of gold to parity with the pound; therefore the theoretical question on the value of gold and its movements plays in Britain such a prominent role; but the question is, whether American bank policy succeeds to avoid this inflation. The most direct and reliable way to the restoration of gold currency in Britain would be a reduction in its paper-money mass. But the British government cannot decide on this reduction, since the latter would be tantamount to a sudden fall of prices of at least 10%, sudden deflation with all its harmful consequences for industry. To a similar effect would lead an extreme increase in interest rates; it reduces not the money mass, but the speed of its circulation. The slowness of the British government to pass the reform, of course, was explained in the first place by these circumstances.

9. Currency and the trade- and payments balances

Let us look at the situation of British currency from the viewpoint of the theory of the trade- and payments balance.

Opponents of the restoration of the gold standard in Britain resort, among other things, also to the argument that so long as the country's trade balance remains adverse, it is dangerous to initiate convertibility into gold.

The question of the relation between the rate of exchange (exchange rates of currency), and the trade- and payments balance is extremely complex and difficult. The reader is referred to the 1924 anthology in which Finn-Enotaevsky provides a summary of new theories of foreign authors and his own work on this subject.[738] The widespread opinion before the war, that the exchange rate of currency depends on the balance of trade, – still during the war the Reichsbank in its official communiques explained the deterioration of German currency by a contraction of export, – Albert Hahn, a supporter of Cassel, rejects in the strongest terms. He argues (following Ricardo) that the commodity price level in the country determinedly affects the height of the foreign rates of exchange, and already through currency onto the condition of the trade balance; [and] that as regards the balance of payments (in the domain of international payment obligations subject to daily maturation), the supply and demand of foreign bills of exchange determines the price of the currency and also only through it already the sum of completed transactions, that is (roughly) the balance of payments. As we

[738][Translated in this volume.]

see, this is the diametrically opposed view, that the trade- and payments balances determine the exchange rate of currency. And Lansburgh argues that the exchange rate may even encourage exports:

> In a country with a gold currency there in practice always and without exceptions was observed, that even a very insignificant growth of the rate of foreign exchange (usually a half, rarely more than one per cent) was sufficient, to level off the balance of liabilities .... gold and more mobile goods (that is commodities) begin to leave abroad, since the growth of the rate of foreign exchange indicates, that abroad one gets a higher price ... the export of gold (and what about that of commodities?) decreases prices in the country, while overseas' prices even more attract all the easily mobile goods.

Thus, there exists an export currency premium also under gold currency. However 'not with the rate of foreign exchange, but in the domain of money circulation within the country' must begin the fight with evil. Lansburgh gives as example of such unsuccessful management of foreign exchange, the experience of Germany from beginning of February to the middle of April 1923, when it, as is known, wantonly threw away 300 million gold mark. This is applied by him also to the present situation of Britain: an increase of the exchange rate of the pound, a decrease of the exchange rate of the dollar will not help Britain, so long as it does not reduce its money circulation. Finn-Enotaevsky maintains from the theory of the 'innovators' that the rate of exchange depends both on the internal construction of the money system but also on the payments balance. 'Ricardo, – he says, – explained the *fluctuations* of the exchange rate, the *violation* of the equilibrium,[739] with the quantity theory of money, and rejected the action of the balance of payments, this was wrong; but the present innovators explain with this theory the (mobile) equilibrium, and the fluctuations – by the balance of payments'. His own position Finn formulates as follows: 'The trade balance and the current account balance (that is, of 'invisible' exports) in times of disturbed international relations and disorder of the money–credit apparatus pressurises more strongly on the balance of payments. ... the urgency of their evening out is reduced, the difference between them and the actual balance of payments diminishes – and one gets the impression, that they directly affect the exchange rate'.

Unfortunately, in this, only in Russian language, booklet on the latest theories of trade- and

[739][In a probable misprint *equilibrium* was stressed.]

payments balances in connection to inter-currency exchange rates the presentation is heavy and indigestible even not only for non-specialists; the controversy is presented much more accessibly and closer to practice in *The Statist*: 'The theory of the trade (and payments) balance, and the gold standard' (21 February 1925). Here is indicated, that concrete facts of the past year contradict theory; according to data of the British Board of Trade, the balance of payments of America became active in favour of America [due to] Britain alone at a size of about $400 million (the 'passiveness' from loans and investments of America exceeded the activeness from its exports of products, but was compensated by income from British loans – $159 million, – and income from invisible exports), [and] nevertheless the dollar fell in the course of that year; on the other hand, the United Kingdom had an 'unfavourable' balance of 106 million (by loans 135 million went away, and income from invisible export over surplus import was only 29 million), [and] nevertheless the pound the whole year rose in exchange rate.[740] In the public debate about the gold standard it was often argued, that Britain is not paying her way (debt) – talk here is not about government debt, but about the indebtedness of the national economy. *The Statist* denies even the possibility of such a protracted unfavourable or protracted favourable payments balance, this is only possible in the short time, and if one takes, for example, one year, it must be remembered, that in the end the debt of the national economy is the debt of individuals, and one would have, perhaps, to assume, that they became all bankrupt. As for the formula 'exports pays imports' then, of course, for imports the individual importers pay, but exporters (visible and invisible exports) are not considered with them; however in a more or less enduring period, the total amount of imports depends on the total amount of exports, that is the payoffs abroad on the payments from there. And from this angle the hypothesis of chronic arrears abroad proves to be impossible. Further, the exchange rate of the pound and the dollar depends on the supply and demand for them on the foreign markets, but this explains only fluctuations in the short term, but in general it is necessary to proceed from the demand and supply of them in their own countries – in other words, *The Statist* puts at the forefront not the theory of payments balance, but the parity theory of commodity price levels or the parity of purchasing power of money in different countries. However, it insists that between the two factors there exists a necessary correspondence. All of the above serves *The Statist* to refute fears, that with the return to gold currency Britain will lose its gold abroad.

[740]In the past year the balance of trade of Britain was the most passive after 1920, import amounted to 1.25 billion, export 795. For the first half of 1925 British import increased by 79 million, export only 4 million.

10. Prices and currency

Let us still dwell briefly on the theory of the parity of the purchasing power of money. It can almost be considered generally accepted in the bourgeois science of our time. We already quoted the words of Cassel that 'in Europe the dollar is valued now below its actual value due to the large American credits to Europe; this kind of rate of exchange is not a reliable basis for recovery of the gold parity of European currencies, this foundation could only be the real purchasing power parity'. The London *Economist*, and with it many other observers argued, – precisely in the spirit of this theory of Cassel, – that the pound rose up in exchange rate because commodity prices in the United States recently grew faster than the British, 'the difference between the British and American prices – and this means: – between the value of money in their countries – soon will be completely insignificant'. This explanation is nearly taken as given by economists in Britain and America.[741]

Opponents of the theory of 'commodity parity' in Germany are Diehl and Elster. The latter mistakenly understands by it not a relation of price levels, but an absolute equality of the purchasing power of money. Finn-Enotaevsky, turning to the classics, recalls that roughly a hundred years ago the theory about different value of money metal in individual countries – was developed by the 'incredible cobbler' McCulloch, and against it spoke already Ricardo. The argument of Cassel, that 'one pays for foreign currency all the higher, the more that the price level is high in one's country, that is, the value of money is low here, and the more that prices in the foreign country are low, that is, the value of money is high over there' – this argument Finn considers to be a tautology proving nothing: pay for money more over there, where it is more expensive.

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[741]However, Anderson strongly rejects this theory. He rejects the dependence of exchange rates on the level of commodity prices and asserts, that, on the contrary, first moves the exchange rate, as the more sensitive factor, and then the commodity prices, as reacting slower. The proof is the period of greenbacks in the United States: changes in the price of gold and the price (exchange rate) of sterling always here preceded changes in commodity prices; in dependence on the changing value of greenbacks firstly changed the exchange rate of sterling and the price of gold, and then only the commodity prices in the United States, and in any case, the exchange rate of the pound was not determined by the 'purchasing power parity', the more so, that British commodity prices remained relatively stable. However, Keynes himself acknowledges in his *A tract on monetary reform*, that 'exchanges are often more sensitive and more volatile than the purchasing power parities' and that 'purchasing power parity is [not always] an accurate forecaster of the course of the foreign exchanges' (pp. 89, 94). Keynes in general often falls into contradictions and, for example, in one place in his *A tract* states that according to the quantity theory the money mass is determined by the level of prices (in fact, this theory argues quite the inverse relation). – Whereas, in the theory of the purchasing power parity of money, high prices of the domestic market are the cause of the bad exchange rate of the currency, another theory assumes the opposite: the bad exchange rate, a premium on gold causes a rise in prices of imports, and following them then also the commodities of domestic production. 'In this way, the premium plays like the role of a protective tariff' (Trachtenberg 1925 ed., p. 281). Perhaps, in this circumstance (also) should be sought the explanation of the hostile relation of British industrialists against the restoration of gold currency; it is clear that a low exchange rate, as export premium, at the same time hinders imports.

However, also from the factual side the increase of the level of American prices, recently overtaking the pace of growth in British prices, remains not entirely proven, and some even think, that British prices rose in recent times, by contrast, more intensely, than American prices. According to *The Statist*, the index of wholesale commodity prices rose in Britain during October 1923 to December 1924 from 150.2 to 174, and according to *Bradstreet's* this index in the United States during the same period rose only from 142.6 to 151. The picture turns here completely reversed. True, it is more correct to take the figures only of the second half of the past year, when the strong rise of the pound took place: in July and December 1924, *Bradstreet's* gives the numbers 137 and 151, and *Statist* 163 and 174; even more favourable for Britain is the index of the Board of Trade; 163 and 170, or the *Economist*: 173 and 180 (all these figures can be compared with each other not absolutely, but only according to their movement).[742]

[put this table in footnote 76]

Price level:

	In pound sterling	In UK (conv. in gold)	In US (conv. in gold)
1924 February	180	160	163
September	172	158	156
October	175	161	159
November	176	167	160
December	177	171	165
1925 January	178	175	168
February	178	174	167

Either way, from the point of view of the theory of the parity of purchasing power of money Britain's chance of emancipation of its pound from vassalage to the dollar hinges on the event that American commodity prices overtake in their upward movement British commodity prices and equalise with them. The issue, however, is not the absolute amount of these prices, but the dynamics of their movement. And this dynamic in recent years shows us

[742]More clearly and correctly from calculations of the bureau of the Federal Reserve:

Table [we do not include this table]

We see that from September 1924 to February 1925; British prices in pound grew half as fast as American prices (6 against 11 points), but in gold, they grew even more (16 against 11 points). Gold prices not only did not meet in Britain and the United States, but, on the contrary, their difference consists now of 7 points, whereas one year ago it was only three points. At that, the difference is not in favour of Britain. Here the theory of Cassel, its explanation of the increase of the pound, limps.

total dependence of Britain on the United States. About this the following summary testifies. At the end of 1919 the American central bank conducted an unheard in history deflationary policy of extreme price reduction; a few months later, in April 1920, Britain was forced to follow this example; the first signs of improvement of the conjuncture appeared in the United States in May 1921, and within a month also British prices correspondingly change. In August 1922 in the United States began an upward movement of prices, and in October we observe the same in Britain; in December there takes place a little reaction in the United States, and immediately it is thrown over to Britain. After February 1923 in the United States a downward movement of prices started, and two months later the same thing happened in Britain; at the end of July of the same year began in the United States an upward movement of prices; the same occurs in Britain; an opposite movement began in the United States in November, and in Britain somewhat later, in February 1924. Every change of the conjunctural curve in the United States is repeated in Britain. 'It is clear that America set the tone, has been the dominant country'. This – is the characteristic recognition in our time of imperialism. The case for Britain stands badly...

Of course, scientific research must show, to what extent these correspondences of the American and British curve are the result of common dependence on the world economy, and how much the lag of the British curve compared with the American is explained by America's primacy in the domain of production or money. Perhaps, in each separate case there will be also specific concrete reasons. We are particularly interested here in the cooperation or antagonism between the factor of prices and the factor of currency. In this complex problem there is still much not clarified.

The most real criterion appears the dearness or cheapness of national production, its influence on the domestic, and hence on the external purchasing power of the currency. As an example, and a very clear one, of the dearness of British production appears the recent order of five motorised ships of 10,000 tons, put forth from Britain to the 'German shipyard' of Stinnes in Hamburg: the latter demanded a price of £15 per ton, while British companies £21, [and] they also stipulated for themselves longer delivery times. This is the largest foreign order of Britain of all times and especially characteristic in our time of unemployment in Britain. This order caused great concern in Britain over the fate of British industry and, in any case, here the currency factor plays no role in comparison with the production.

Consistent application of the theory of commodity parity or purchasing power of money – leaving aside the question about the value – would have to in the first turn proceed from the

different production conditions in these countries: herewith should be resolved that difficulty, that in countries with advanced technology commodity prices are lower than in countries underdeveloped in this relation, and cheap commodities means here, according to this theory, dearness of money, but, on the other hand, facts show, that precisely in the countries with developed technical production money is cheaper, than in underdeveloped capitalist countries.

The issue of scientific analysis is to explain the inversely-proportional correlation between the pound and the dollar, to explain, why the decrease in the dollar led to an increase of the pound, although in an interval of a few months after the increase in American prices there followed a rise of British prices? In the existing discussion many measure the gold exchange rate of the pound via the dollar, but meanwhile the dollar itself is also subject in this case to measurement; it is necessary to determine, whether we have in every given case a change of the pound or a change of the dollar (or both), – in other words, for example, whether the pound falls or the dollar falls, whether the rise of the pound is independent, a real phenomenon or just a reflection of the dollar's slide? It is possible, that the stabilisation of European currencies, and in the first place the pound, is in fact only an echo of the fall of the dollar... According to the index of Irving Fisher, the purchasing power of the dollar fell from 69.1 in the second quarter of 1924 to 61.3 at the end of February 1925. *Nota bene*: depreciation of the dollar, which is expressed in these figures, is depreciation in relation to commodities, not in relation to gold. The issue of concrete scientific analysis is to show, further, on each individual case, whether there is present an actual or an inflated rise of industrial conjuncture? According to the theory of purchasing power parity of money, a rising American conjuncture, insofar as it increases American commodity prices, should lead to a higher pound against the dollar; in other words, a strengthening of the United States in the domain of production should be accompanied by a weakening of it in the domain of currency.[743] Is there here not some mistake? Does not the parity theory apply only to inflationary phenomena? It is necessary to analyse and figure out also the following contradiction: on the one hand, the conjuncture curve in America is repeated, albeit with some minor delay, in Britain, but, on the other hand, the rise in America, the increase in American commodity prices is reflected in Britain in a rise of the pound, and consequently, the difficulty of sales abroad – in other words, the currency improves, but the production and trade position of Britain worsens. Or the reverse: should an increase in American prices

[743]Here it is necessary to take into account also the following moment. An increase of prices and conjuncture in America leads usually to a reflux of American capital from Britain to America, and therefore, does not raise, but lowers the pound. This complicating moment operates counter to the theory of parity.

improve British export? How is manifested the eccentricity[744] of the external and internal purchasing power of currency? In gold and commodities… What game of interests of money- and industrial capital reflects these interactions and contradictions?

Let us repeat: to completely cover, and even less to give an analysis of all these problems is not our task. About the purely–theoretical side of the theory of parity of power purchasing power of money we do not consider [it here] possible to expand. We are interested here only in concrete facts and conditions in connection with the imperialist reality of our time, in particular with the struggle of Britain and the United States for domination on the world money market. Let us note just still the following. With regard to the antinomy of money- and industrial capital, the theory of parity of purchasing power of money, insofar as it proceeds from commodity price levels, would seem, to have some pluses before the endlessly emphasised exclusively money side, in particular the panacea of the bank rate, with which Cassel and others err. But the instigators of this theory have managed to reduce also this plus. They portray this theory in such form, that the commodity price level is only a derivative of bank policy. So, for example, the increase of the level of American prices for the second half of the past year on average by 10% Keynes explained thereby, that at this time New York banks increased their credits to the public by 30%, in London the price and quantity of loans and deposits in banks remained stationary and therefore commodity prices rose only 4% and the result was an improvement of the exchange rate of the pound by 8%.[745] As we see, the price level from the first factor is here turned into a secondary one. In this relation one goes still farther: the increase of American prices would show not only the hand of the credit policy of American banks, but almost the result of simple political manoeuvres – so, for example, *The New Statesman* and many others contend, that before the election of Coolidge American banks received the determined directive to extend loans and thus create a boomlet, a small uplift, to capture the votes of farmers; let it be so, but an increase in American wheat prices occurred for quite objective reasons [like] the poor harvest, and especially due to the fact that the USSR temporarily was forced to act as a buyer on the world market of bread-grain.

In short, the theory of the parity of the purchasing power of money, – whether true or not theoretically, – is used here not on the ground of production basis, but constructed solely on the primacy of banks and money capital. In this is manifested the same antinomy between industrial and money capital, which we emphasised at the very beginning, still with examples from the period of the Napoleonic wars. No wonder, that the last increase of the

[744][In mathematics, a measure of how much the conic section deviates from being circular.]
[745]Keynes 1925b.

rate of the Bank of England called forth on the pages of *The Times* bitter complaints of the by us already quoted Sir Josiah Stamp in the spirit, that this increase was not due to natural, organic needs of British industry, but, on the contrary, to the detriment of it and exclusively from money and currency considerations, as a response to a similar step of the United States. The venerable Sir says that Britain 'obeyed the crack of the whip of America', that because of this the British industrialists abide 'in a constant fear and unnecessary nervousness' and asks himself, 'have we become a vassal of America', fearing the conclusive enslavement of the pound to the dollar. This is the same antagonism of interests of industrial and money capital, the same alternative: price stability or currency stability, the same antinomy, which still in 1819 was formulated in Peel's Committee as follows: do the advantages to industry from the confidence, that the pound will be restored to a gold basis, exceed the disadvantages of the credit reduction and lower prices? On the complaints of Stamp, that the Bank of England in its discount policy does not consider the needs of British industry, *The Times* entirely reasonable says, that if British industry could have been helped by discount and loan rates to get out of the difficult situation, then this would have been not yet so bad... This time, this panacea is no longer presented. The masks have fallen. The question about the primacy of money capital over industrial capital has been squarely put.

11. Prospects

On 28 April 1925 Winston Churchill introduced in the House of Commons and soon after both chambers accepted in all three readings the 'Act on the gold standard', a bill 'on facilitating the restoration of the gold standard and achieve objectives related to it'. Churchill spoke with the to him proper theatricality and effectiveness. This step was not slow to produce the due impression on world markets and in the world capitalist press. It was acclaimed as 'the last link in the conclusive stabilisation of the world economy after the war', the American press placed a portrait of Churchill with the inscription: 'the one who leads Britain to payment ability' and so on. Thus, the Rubicon crossed, the British government, having manifested in recent times some slowness, finally, decided. However it furnished the new law with so many restrictions and so many special measures of precaution, that it, perhaps can be more taken for its opposite, it so significantly cuts down the regime of gold currency, that it more resembles a formal rejection of it.

The new law formally releases the Bank of England, going forward, from the obligation to convert banknotes, as well as *currency notes* into gold. Meanwhile Britain, almost one and a

half century, until the seventies of the last century, formerly was the only country in the world with a gold currency, even in the time of world war it formally did not cancel convertibility into gold; it only factually disappeared, since private demand for convertibility was regarded as an attempt of illegal export of gold abroad. Further, the new law requires the Bank of England to sell gold at the prewar coin parity – £3 17s. 10.5d. per ounce (as we know, this firm 'price of money' has two centuries of standing); however these sales should be made not in coin, but only in bullion, wherewith only an amount of not less than 400 ounces (12.4 kilograms). Of course, this latter restriction aims to reduce the possibility of purchases of gold from the Bank by private persons. As for the obligation to sell gold not in coin, but only in bars, it signifies that gold circulation is restored only in the relations of Britain to abroad, but not at all in Britain itself. The Committee of experts on whose report the new law was based, specifically expressed (in point 43), that 'the use of gold for domestic circulation is a luxury which can well be dispensed with, and which we are in fact, at any rate during the next few years, not likely to be able to afford'.[746] So, in the near future Britain introduces, essentially, only a system of 'currency with a golden core' (*Goldkernwährung*), having singular success in pre-war Austria, and now more and more spreading. Under this system gold is stored in the central bank and serves only for the purpose of currency and foreign exchange policy (management). But meanwhile until the world war the British money system was built on exactly the opposite principle, that, except for a small amount (about 18 million, composed of government debt to the Bank of England), for all the remainder has to issue banknotes completely covered by gold; Britain upheld this system, despite the fact that the experience of other countries showed its needlessness in such strict form. All the more significant is the present law. However, something similar to it was proposed already by Ricardo in his *Proposals for an economical and secure currency*; he, too, proposed to oblige the Bank of England to convertibility of its banknotes into gold bars of 20 ounces, but not into coins; this proposal was not accepted. Further: according to the new law, the right to mint coins also remains the monopoly of the Bank of England, but this time already not merely de facto, but formally institutionalised. Finally, allowing already before the expiry of the ban, which is not expected to be renewed, the free export of gold abroad, the new law allows it not at all to everyone, but only to the Bank of England. The law contains also authority for the Treasury to conclude for the strengthening of the currency special loans of terms up to two years; already now Britain enlisted the support of America from the side of the New York Federal Reserve Bank a readiness of a loan of $200 million and from the side

[746]Committee on the Currency and Bank of England Note Issues, 1925.

of the Morgan bank $100 million; this will be the intervention fund.
Some are inclined to attribute to this step of Britain only the significance of psychological stimulus. 'If we [Britain] – Sir Robert Horn said during a debate in Parliament [4 May] – who regard ourselves as the centre of the world's (sic) financial system, refuse [the restoration of gold currency] and declare, that we that we were not ready to take this momentous step, it surely would be an extraordinary confession of weakness and would have a most adverse affect ... upon the value of our sterling in the exchanges of the world'. Thus, a question of prestige... The report of experts (point 20) also says that if the decisive step will not be taken, then the .. 'psychological causes which have operated to force the pound up will tend to act in the other direction'. 'If the English pound sterling is not to be anchored to the standard which everyone knows and can trust, and which everyone in every country understands, and can rely upon, the business, not only of the British Empire, but of Europe as well, might easily have come to be transacted in dollars instead of in pounds sterling'. Of course, this lapidary exaggeration belongs to Churchill [4 May, parliament]... He spoke also as regards the dependence on America.

> We are told – he said, – that the gold standard will put us in subjection to the United States, [or] that we shall be shackled to them [even more]. ... [However,] our interests [were always] profoundly and intimately involved in those of the United States ... Therefore it is not a question of whether the return to a gold standard makes us dependent on the United States, but whether it makes us more dependent or dependent in an unhealthy and a subservient manner. ... We are often told that the gold standard will shackle us to the United States. [Well,] I will tell you what it will shackle us to. It will shackle us to reality.

As the reader sees, the Chancellor of the Exchequer found only superficial beautiful phrases, but not arguments on the essential.
During the debate in parliament the main knots, raising concerns of the opposition, were questions about the flooding of Britain with American gold, that is about gold inflation, and on the other hand, about the prospect of deflation. One must say that these issues have remained open. Churchill, this new-titled saviour of the fatherland, showed the him affecting ignorance and carelessness. In fact: on 4 May [in parliament] he said that he did not at all fear a 'flooding with gold', that, '[if it took place], all the Treasury would have to do would be to float an internal loan, purchase the gold and remit it to the United States in cancellation of the War Debt'. But just a day later, 5 May [third reading], the same Churchill, without batting

an eye, says in completely opposite spirit: 'Supposing enormous quantities of gold were hurled upon us, poured upon us from every quarter; [and] we were being smothered under an avalanche of gold, I say without hesitation that we should have to legislate [to seriously fight against it]'. As for the argument of Churchill, that in the event of an extreme influx of gold from the United States into Britain the latter will be able to use that cheap gold to pay its debt to the United States, Keynes showed that here there is a simple mistake, because we are talking about the influx of gold from America in the form of temporary loans, and it is clear that to cover one (war) loan from other loans, at a less favourable interest rate, is not at all a relief for Britain. Keynes considers it a big mistake, that the new law did not cancel Art. 4 of the Bank Act of Peel, obliging the Bank of England to buy gold in any amount offered to it at the fixed price of £3 17s. 9d. per ounce. This, he said, would save our pound from the necessity to follow gold in case of a catastrophic fall of the latter. Of course, the bringing of the pound to gold parity significantly facilitates the flow of gold into Britain; but in the fears of a catastrophic fall of the value of gold is manifested, in the main, a theory, those views, about which we spoke above and which contributed to the post-war devastation. Keynes casually mentions even the possibility of a chemical revolution in the production of gold, and the press also entirely determinedly points to the discovery of professor Adolf Miethe, although this, of course, is absurd, since to make from mercury a gold dollar is tens of thousands times more costly than this dollar.[747] The real background of the fear of a fall of gold is only the enormous accumulation of it in the United States. But in general it is necessary to recognise, that on this in the current debate reigns a decent confusion: on the one hand, in Britain one fears the leaving of its gold, on the other hand – an influx of gold. On one side, fear of a fall of the value of gold, that is increase of commodity prices; on the other, the same Britain fears most that the return to the gold will lead to a decrease in commodity prices... *The Statist* of 9 May expects in the near future a rise of commodity prices in Britain and in this sense welcomes a 'gold inflation'. We see: full discordance, largely built on unsubstantiated claims.

On another sore issue, namely on the prospect of deflation, we find the same web of contradictions. Churchill, of course, appearing before parliament with all considerate official optimism, assured, that the government does not see any necessity in deflation and in an increase in the near future of the bank rate. Churchill in general indiscriminately denies the danger of the situation. Herewith he also, however, categorically breaks with the conclusion of his own great governmental experts, serving as the 'scientific' basis for the bill. This is the

[747][This experiment's result gathered no scientific acceptance.]

so called Committee on the Currency and Bank of England note issues; the conclusion of the Committee consisted of 50 points, dated February 5 and signed by Bradbury, Gaspard Farrer, Sir Niemeyer and Pigou.[748] In point 19 these experts say: 'The discrepancy between British and American gold prices which existed in September has not disappeared, though it has been reduced. We must still be prepared to face a fall in the final price level here [in Britain] of a significant, though not very large, amount, unless it should happen that a corresponding rise takes place in America'. However the government stood in parliament on the opposite, soothing viewpoint. In point 32 the experts determinedly say that to bring the British price level in conformity to the free gold market there needs to be a reduction of loans; this is equivalent to an increase of the bank rate, an increase, the necessity of which is denied by representatives of the government. Point 13 also provides: 'A free gold market could readily be established and maintained at the pre-war parity, provided that by control of credit we adjusted the internal purchasing power of the pound to its exchange parity, and restricted our foreign investments to our normal export surplus'. It is clear that under the control of credit here is understood reduction of it, in other words, the so undesirable for industry deflation. Moreover, not only the government – at least in words – is at odds with its experts; the report itself is interwoven with contradictions, the whole is built according to the system: on the one hand it is difficult not to recognise, but on the other one must admit. In point 15 it speaks about the prospect of lower prices by 10-12%, in point 20 this is already only 1.5%, and so on. In point 17 the experts say that they would rather like to wait, than to reduce prices, but in the following paragraph they find, that the favourable exchange rate nevertheless motivates one to use the situation for the return to gold currency. How then could opponents of this step not argue, that it is built on shaky ground, on artificial foundations. But most characteristic is point 32; in it the experts refer to the experience of the restoration of Britain of the gold standard after the Napoleonic wars, as well as [that] of some states of the European continent in our time: '[which has] shown that a courageous policy in currency matters surmounts apparently formidable obstacles with surprising ease. We believe that on this point history will repeat itself' (sic). No wonder Philip Snowden on behalf of the opposition protested in parliament against the 'undue precipitancy', with which the reform is carried out; however, he took his proposal, in the end, back. Usually Britain featured a thoughtfulness of its policies. True, the government now primarily pursues exclusively the interests of its currency and money-, perhaps even commercial capital; it sacrifices the interests of industry and tries to disguise this with beautiful phrases. Moreover,

[748]Arthur Pigou, considered one of the best British economists, participated also in the Cunliffe Committee.

as we have seen, the new law was furnished with all sorts of precautions. But from all the by us given contradictions, we can draw the conclusion, that – whether or not Britain succeeds to conquer its former position on the world money market – here in front of us is a bright example of the decadence of post-war capitalism: even such a serious measure, as the restoration of gold currency in Britain, even that crown of world stabilisation is held haphazardly, gropingly, in contradiction with its own experts, under full discordance of the scientific representatives of capitalism.[749]

This discordance cannot be explained only by opposing interests; for example, the prediction of an exodus of gold or its influx, decrease of prices, or their increase is so 'piquant' in its contradictoriness, that there is only one conclusion: modern decadent capitalism itself does not see its immediate prospects, walks blindly.

The Act of 1870 on free coinage is now cancelled in Britain. But, nevertheless, the question of the further fate of gold troubles theorists and practitioners. McKenna believes that the supply of gold at present prices will be enough for the world for many years; Cassel, on the contrary, believes, that the demand for gold is growing faster than its production. To prove one or the other is impossible. India remains a very uncertain factor:[750] the import of gold into India rose from Rs. 30.4 million in 1919 to 392 million in 1923, but it varies greatly and, moreover, with it competes silver. America imported in 1924 $258 million more gold than it exported; this, despite the huge jump of its overseas investments in 1924. Only in 1925 it has an excess of gold export over import; for the first 3 months $131 million. Either way, this means, that it was able to 'float' only a fraction of its gold (by gold loans of the Dawes Plan), and that the talk about instability of the value of gold is not 'grey theory'; the 'revolution of gold' is far from outdated. In Europe there is a shortage of $2 billion gold, while in America, according to the account of Kemmerer and Vissering, a similar excess. Meanwhile both

[749]Although to the latter definitely does not belong the, speaking in the House of Commons followed by Churchill [second reading of the Gold Standard Bill, 4 May 1925], Financial Secretary to the Treasury, a certain Colonel Walter Guinness, his speech was so characterised by his helplessness, that we give it to illustrate. First of all, this gentleman announced, that experts gave the government the most soothing assurances. Then he said: '[The right hon. Gentleman (Mr. Wheatley)] fears a return to the gold standard on the ground that it might lead to a higher Bank rate, and ... cause higher prices. We hope that there is no real danger of any such effect on the Bank rate, but, even if he were right, we believe that the result on prices would be the exact opposite from what the right hon. Gentleman has suggested, because it is both in accordance with all the accepted theories on the subject and also with the recent experience in this country and in the United States that a rise in the Bank rate is immediately followed by a fall in wholesale prices'. Here is already quite a Babylonian pandemonium. Firstly, the opposition fears from the new law not an increase, but precisely a decrease of prices. Secondly, the 'accepted theory' does not meet objection also in the opposition, it precisely also proceeds from it. Thirdly, Guinness declares, that 'there is no real evidence ... of price readjustments in this country in response to price levels in the United States'; whereas the report of experts, and all authorities in Britain believe a possible rise in prices in America is only a plus for Britain! Obviously, the representative of the British Ministry of Finance is much more competent as a colonel than as financier. These lapses of him are so obvious that some London newspapers deleted them, but other newspaper gave them.

[750][Arzet 1925, p. 184.]

theorists and practitioners emphasise, that in order to restore the normal course of the world economy first a redistribution of gold on a world scale is necessary.

To Philip Snowden, Chancellor of the Exchequer in the MacDonald cabinet, belong the following winged words: 'Only two people understand the meaning of inter-currency exchange rates; but one of them died, and the other is in an insane asylum'. Such confession, in any case, is very characteristic from the mouth of the Minister of Finance, furthermore of the same power, claiming still as before the role of financial hegemon of the world. Of course, there is a share of truth here in the sense, that this is an extremely complex and difficult problem, one of the most difficult, if not the most difficult (and therefore also interesting) in all political economy.[751] But we emphasise here, that it is not by chance that now these problems have surfaced with all their confusion; this is the result of the world war and the post-war ruin of the world economy. Precisely they make questions of currency topical. Hitherto, when capitalism was not yet derailed, questions such as the difference of internal and external purchasing power of currency, could be only of theoretical interest, but also theory did not advance them, since practical life almost did not know of such discrepancies in more or less strong extent. Theoretical bewilderment is in this case a true reflection of the real instability of post-war capitalism. In the question about the stabilisation of capitalism the currency problem has not yet said its last word, and in this respect it is of special interest for us to await the results of the recent British experiment. Will in fact this experiment, in which, as we have seen, there is, despite all precautions and all curtailment, such considerable element of risk, complete the stabilisation of the world economy and restore the prewar role of Britain? Or, on the contrary, will it create only new difficulties, new contradictions: strengthen instability on the basis of the oscillation of the value of gold, the leaving of it from the country or an excessive influx, [and] throw Britain into bondage to America? It is possible that it fashions in Europe two close-knit currency fronts: countries with a gold standard under the leadership of Britain and countries with a sick currency, namely France, Italy, Yugoslavia, Romania and Bulgaria, where these latter sooner or later will be forced to begin devaluation of their currency, and the restoration of gold currency in Britain will only push toward this. One can imagine that a devaluation of the franc would pass in France far from completely painless and cause new and major upheavals on the domestic and international scale.

But apart from all this – and, presumably, still more importantly – the restoration of the gold

[751]'Gladstone, speaking in a parliamentary debate on Sir Robert Peel's Bank Act of 1844 and 1845, observed that even love has not turned more men into fools than has the meditation upon the nature of money' (Marx 1987, p. 303).

standard in Britain promises to be a hotbed of acute social conflicts and in this regard directly touches the interests of the proletariat, in the first place the British. The latter will come to test on its own back the results of the 'reform', meant to stabilise and lift up British external and in general world trade, but, for now, as we have seen, there threatens an exceedingly burdensome deflationary reduction of prices, wherewith this reduction will not only affect a stagnation of British industry, but will, in time-tested manner, be conducted mainly through a reduction of wages. Among the heralds of the latter appear the already surveyed bourgeois economists, seemingly, at first glance [to be] innocent and objective. In the commercial supplement to the *Manchester Guardian* of 30 April Cassel calculates, that in February 1925 the foreign purchasing power of the pound (exchange rate) was 4% higher than its internal purchasing power; this difference is actually a premium on the import of foreign commodities into Britain and on the export of gold from it and eliminating it, as Cassel stresses, is possible only by an increase of the internal purchasing power of the pound, that is by a decline of British prices. In the May issue of *The National Review* one of the eminent bankers of the City, J.F. Darling, placed an article under the title 'America or (the British) Empire?' which opposes the restoration of the gold standard and argues, that, due to the lagging of the internal to the external purchasing power of the pound, debtors in America now profitably send their commodities to Britain, getting there for them pounds and change these for dollars. Keynes in the London *Nation* of 9 May [1925d] and in *The New Republic* of 6 May, also dwells on the discrepancy between the internal and external purchasing power of the pound, wherewith he comes to particularly interesting results for us. If – he says – Britain exports its commodities for one dollar and then converts this dollar into pounds to pay its workers, the latter can buy with them far fewer objects of their consumption, than in Germany, France or Italy; the cost of living in gold has risen in Britain far more than in the rest of Europe, and this means, for Keynes, none other than the fact that the purchasing power of the pound in life necessaries lagged behind its golden parity. Keynes stresses, that this discrepancy is especially strong in relation to objects of consumption of workers. Thus, already here we have very unpromising results for British workers. But this is only the beginning. Keynes divides all commodities into three groups: such as, cotton and raw materials, comprising the subject of international trade mainly, then fabricates like textiles in a lesser, but also still very significant degree comprising the subject of this trade, and finally, household [objects] etc. and in particular 'services'; the latter group is the least susceptible to the influence of external trade – to 'services' he reckons wage labour. And now, it is not difficult to guess what conclusion follows from this according to Keynes. Since wages

are least of all subject to the above mentioned nivellating influence, hence the discrepancy between internal and external purchasing power appears mainly in the height of wages, and in the first place to recover the balance Keynes considers a decrease necessary of British wages, herewith in the size of a whole 10%; in this he also sees an inevitable result of Britain's return to gold currency. These are the concrete and so significant results of the interaction between the currency and commodities markets. True, in places the statement of Keynes is not entirely intelligible and not free from contradiction. For example, when he assigns to the third group consumption objects of workers and demands of them a reduction of prices by 10%; but these consumption objects consist, primarily, of import of food and, seemingly, are subject in high degree to the levelling action of foreign trade, which manifests itself in the fact, that if on the domestic market the prices of them in gold are above world prices, then into the country pours a flow of these commodities. Next Keynes reassures, that the difficulty of Britain in competition on foreign markets arises not at all not from high real wages in Britain (in America, as Keynes rightly indicate, they are twice above), but only from the inappropriately high cost of living in gold in Britain; nevertheless, he believes wage cuts necessary and unavoidable. Only in gold. But while the real wage adapts to it and returns to the previous level (because, of course, the decrease will be reflected also on it), the horse starves.[752] Either way, the scapegoat is the British working class. This shows what worth have the sweet assurances of the representatives of the British government under the readings of the new bill in the House of Commons, that there are no grounds to fear deflation and that the contradiction of interests between industry and the banks in the question on the gold currency – is a myth. The return of Britain to gold currency opens before the British workers an era of new and extremely severe social conflicts. And the prospect on a world scale, as we have seen, likewise is far from rosy.

In conclusion let us briefly touch those new facts, which occurred after the publication of the British law on the gold standard. The circulation of banknotes of the Bank of England, which amounted to a monthly average in 1924 of £125.4 million, rose in May 1925 to £147.8 million. The quantity of *currency notes* of £287.9 million (average figure for 1924) rose in May 1925 to £291.2 million. In general, in money circulation there was felt stronger stress. Overall the amount of deposits in the Bank of England of £139.7 million in December 1924 fell to £119.8 million in May 1925, and deposits in other London banks from £1696 to 1645 billion. With regard to the amount of gold in the Bank of England, its movement is characterised by the following figures: from April 30 to May 20 from the Bank's fund

[752][While the grass grows, the horse starves.]

£2,334,000 gold left, while it received £2,525,000 gold, namely on 15 May 1,610,000 and on 20 May £900,000, wherewith in respect to the first amount one surmises that it was sold to the Bank of England by the Bank of France, and with respect to the second, that it came from the USSR in connection with the procurement of commodities. As on 20 May the pound stood at 4.86 3/8 (the maximum since 1914), and 'the highest gold point' of 4.9067 it did not reach, then the acquisition of the sums of gold was associated for the Bank of England with important sacrifices, this was not a regular inflow of normal times. On 15 July 1925 the gold reserve of the Bank of England totalled £161.6 million, and the net inflow of gold for 2.5 months was £5.7 million.

In mid-May on the London market there was a fiasco of such safe and small loans as [those of] the government of New Zealand of £7 million and even the London County Council of £6 million, whereas at the same time the New York market in a few days deployed easily a loan of $85 million for one car company.[753] In the first half of 1925 the voluntary and involuntary abstinence of London from issuance of long-term credits appeared even more starkly, than in 1924. In July there were held negotiations of a great loan for Australia on the American market of $100 million, wherewith *The Times* (10 July) not only does not scream blue murder about this separation of the Dominion from the metropolis, but was forced to put up a good face on a bad game and praise Australia because 'she looked openly in the face of the situation and decided to float part of the new loan in America'.

At the same time as Britain returned to gold currency [so did] Australia, New Zealand, South Africa, the Netherlands and Dutch India. In May the Argentine government allowed the export of gold. The Chief Cashier of the Bank of England Sir Ernest Harvey arrived in May in Helsinki for talks with the Bank of Finland: the currency reform in Finland is carried out in close connection with the Bank of England (and the political background of this currency colonisation is quite clear); the draft bill on this reform should be proposed to parliament in September 1925. But it is curious, that the proposed exchange rate of the Finish mark is fixed in the present relation to the dollar: 39.7 mark equal to $1. In Hungary, in connection with the British reform, the question on currency reform entered into an acute stage, wherewith the proposed reform is based on the pound sterling.[754] It is significant, that the new domestic loan of [Minister of Finance] Caillaux in France, providing for interest payment in hard currency, is based also on the pound. The issuance rate of these gold bonds is based on the value of the pound at 95 francs (actually it exceeded already a hundred and on the world markets already there is dispute, whether in the relation of the franc to the pound the

[753][Arzet 1925, p. 177.]
[754][Cited from Arzet 1925, pp. 178–80.]

impending devaluation of the franc is not already a foregone conclusion). Very significant was the visit to Berlin in late July of the Governor of the Bank of England Sir Montagu Norman; some bring it in connection with the negotiation of the Dawes Plan, while *The Daily Herald* (24 July) reports very sensational and still to be verified news, that the Bank of England offers Germany a loan of 40 million, provided Germany consents to the demands of the Allies with respect to the guarantee negotiation. Britain hardly is now in a position to give such a significant credit to Germany, but the connection with politics, in any case, is characteristic for such 'currency imperialism'.

Decamps in *Les changes étrangers*, p. 376 gives a summary of the theoretical- (by changes of the price level) and the actual exchange rate of the franc to the dollar for 1919-1920-1921; deviation of the actual exchange rate from the theoretically calculated one was very insignificant with him. In *The Financial News* (27 March 1925) appeared a piece by E.J. Lake about the commodity parity,[755] in which on the basis of British and American indices for 1919–25 was calculated, what should be the theoretical exchange rate of the pound in connection with the level of commodity prices in the two countries and how it was actually. In this case there turned out to be great divergence in various directions: for example, in March 1921 theoretically 3.50, actually 3.90, in September theoretically 3.95, actually 3.71. The biggest divergences were during the whole of 1923, the largest convergence from September 1924 to February 1925. Dr Arzet believes therefore, that a possible increase of American prices is not identical with a fall of the dollar on the European markets, but [rather] with an increase of also the European price level. 'From the supervision of the price movement one will not bring about, therefore, that stability in currencies, which is [longed for by all countries and] expected [in theory, from a return to gold]. Only the stability of the gold price itself can serve in the future as guarantee for the constancy of international price relations'.[756] Edwin Cannan too argues that, under a gold standard, 'the currency policy of the single nation can no longer affect the purchasing power of its money',[757] an increase or decrease of the purchasing power of bullion must be reflected on all countries. This – sharp rejection of the possibility of influencing a gold currency (likewise by discount policy), is the direct opposite of the theories of Keynes and Cassel.

Already after viewing the proof sheets (July 1925) it was reported that 'at the last minute' Britain managed, though with difficulty, to assume a quarter of the Australian loan (25

[755]['Test of Purchasing Power Theory'. Cited in Arzet 1925, p. 182.]
[756]Arzet 1925, p. 183.
[757]'The Gold Standard', *The Times. Imperial and Foreign Trade & Engineering Supplement.*, International Banking Section. 23 May 1925. ['except in the trifling degree in which it can affect the purchasing power of bullion in the world, by slightly increasing or decreasing the total demand for it'. Cited in Arzet.]

million). In addition, the published figures for issuance for the first half of 1925: in the United States $4421 million (nearly £1000 million), of which 1073 for abroad, including 676 for Europe, issuance of Britain only 112 million, from which only 5.1 million for abroad. According to the index of *The Statist* by the end of June 1925, British prices fell over six months more than 10%; in June they fell, while in other world centres with a gold currency they rose. Thus, concerns relating to deflation, evidently, were quickly confirmed. If *The Statist* considers the link between this decline of prices and the Bill on the gold currency unproven, the opponents of the law see it almost as the culprit of the present acute crisis in British industry.

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Already at the time of printing of these pages the discussion in Britain resumed and is again in full swing. We can note only a few of the most important points. On 6 August the Bank of England lowered its rate by half a per cent. For many this was a complete surprise and it is at present still impossible to determine the full significance of this fundamental fact from the domain of 'interest rate war'. Even such informed organ as the *Manchester Guardian* wrote in late July: 'If the development on the money market, indeed (under the influence of the influx of gold) will lead to an enduring decrease in the money rate and that makes topical, contrary to expectation, the question about a decrease of the bank rate, then it must be assumed, that in such case in all likelihood the 'embargo' (prohibition) of foreign loans will be withdrawn, rather than a reduction of this rate'. The subsequent, nevertheless, decrease of it goes against all that we have seen above, and does not fit with the present plight of Britain. Only the autumn turnover of the market should show, to what extent this decrease was correct. The influx of gold over 3 months was 8.5 million, about which boasted in one of his recent speeches Winston Churchill, and the coverage of the banknote and the pegging to it under the new law of *currency notes* by almost 40% can only partly explain such sharp turn toward optimism, especially since this influx is not enduring and mainly, the result of artificial measures. Incidentally, (evidently by prior agreement) the Bank of the Netherlands buys promissory notes in sterling from revenue of the sale of gold. To claim, that the decrease of the bank rate happened only, as a calming manoeuvre, is also risky. Most likely, this reduction is not so much a sign of a favourable situation of the British money market, as a sign of the difficult position of the whole British industry and trade, being manifested in the reduction of discounts: five large London banks (as well as five small clearing-banks) had on 30 June 1922 a figure of 248 million discounts, but 30 June 1925 208 million as the result of the sluggish state of industry. Loans of these banks true, increased for the same time from

808 million to 867 million, this also calls forth surprise, but *The Times* (23 July) explains this by the growth of import and internal trade.

On the loan of Australia let us still remark, that the English part of it was covered only within three days, whereas, for example, on 2 June the Morgan bank and the National City Bank within one hour with excess covered a loan of the Argentine government of $45 million (that is almost twice the English part), and a few days later, the American bank Blair & Co. in a quarter of an hour underwrote a 30 million loan of Norway. If in 1924 American investment in Europe rose from 20% to 60% of the total number of foreign investment of the United States, then the breakaway of Australia from the metropolis is still more sensitive for Britain. In the press optimists console themselves with the fact that the loan of Australia in America goes to the payment of Australian debt in Britain, but Keynes, on the contrary, indicates that as a result of this loan Australian orders leave Britain (they were usually based on British loans). Keynes sharply attacks the government, on the ground that the imposed embargo greatly reduced British lending not only abroad, but also to the Dominions and colonies. However, the twists and turns of the Australian loan show, that the problem is not just in the money *policy*, but in the actual ability: the concluded loan was deliberately delayed and finally the London market just barely mastered its part.

In connection with the catastrophic position [that] Britain's coal industry is suffering, threatening in early August a grand strike, opponents of the move to gold boil down the crisis of British industry almost exclusively to the result of deflation. This, of course, is one-sided. Keynes released the pamphlet *The economic consequences of Mr. Churchill*, in which he gives the following figures: in March 1924 the index of the cost of living was 178 on the basis of the paper pound and 157 on gold basis, and in the United States 156, [while] now in Britain it is equal to 173 (the same in gold or in pound), and in the United States 153. In other words, in Britain the level of commodity prices is now exactly 10% higher than in the United States (173 and 158). Hence Keynes draws the conclusion about the inevitability of a decline in British commodity prices and primarily wages by as much as 10%, to fit the former British prices in paper pound to the new prices in gold, to the prices of the world market, or put differently: to fit the internal purchasing power of the pound to its external purchasing power or exchange rate. Thus, the demand of a reduction of wages meets here, so to speak, scientific support. In fact, however, the export of British coal falls not only because of its high cost. Keynes consoles, that with a decrease in all prices real wages remain on the previous level. Keynes emphasises that all his pessimist predictions of inevitable deflation completely and soon will materialise into reality due to the situation of the export of coal, and so on. In

the same spirit Josiah Stamp argued in his report to the Commission surveying the coal industry.

Churchill is trying to defend himself, and argued recently, that 'it is more frank to impose on the taxpayer direct aid to the coal industry in the form now adopted of subsidies, than to take of him the same money in the form of a hidden export premium under a low exchange rate of the pound'. Sir Henry Strakosch and others dispute the correctness of the comparison of indices, calculated on a variety of bases; but Keynes himself knows this and stipulated in the sense that the actual ratio should be even less in favour of Britain.

Thus, the present industrial crisis in Britain manifests in bright form our antinomy between the interests of money capital (currency) and industrial capital. Even without solidarising with the exaggerations of those who boil down the crisis of industry to a monetary factor, to deflation, one cannot avoid seeing the important symptomatic meaning of this counter-position. This antinomy affects also the policy of the conservative British government in relation to Soviet Russia: it sacrifices the interests of British industry and the exports, needed in the development of trade with us, it sacrifices for the sake of interests if not of purely money-, then at least of finance capital, putting in the first place the payment of debt.

Let us still note the work of the Russian author Abrosimov: 'Toward a theory of the exchange rate (In defence of the theory of commodity parity)', appearing in the Harbin *Vestnik Man'chzhurii*. – The author determinedly takes the side of the theory of Cassel and Keynes about the level of commodity prices (commodity parity), a theory, laying at the basis also of the just listed by us considerations of Keynes. 'From the fact – said Abrosimov – that the ruble buys about 0.002 dollar, but first bought 0.5 dollar, it does not come about that Russia gives more of its commodities for commodities of the United States (if that exchange rate corresponds with the commodity parity), just as it is not necessary to spend at a tailor more cloth on an overcoat with the transition from the meter to the arshin [71.12 cm]. Important is not the absolute value of the rate of exchange, but its correspondence with the commodity parity'.

Moscow, 14 August 1925.

Chapter Twenty-Nine

The Collapse. The Credit Crisis in England (21 September 1931)

Rudolf Hilferding

In 1924 Hilferding wrote in a letter to Kautsky:

“I myself barely arrive at scientific work, although two things constantly float in my mind. One is an elaboration of my money theory and simultaneously a critique of the latest English and American crisis-, banking-, and money-matters, which, while perhaps not theoretically significant, practically are very interesting. Namely the problem of the influence of the credit policy of the central bank on the industrial cycle. The other is a 'Political theory of the state', which also practically can be very significant.”

Of course Hilferding did touch on money questions which the economic situation put to the front. On the internal handling of the crisis in Germany, which preceded the English one, he wrote in August 1931:

“... [T]he mistrust of abroad has reproduced itself domestically. The gold outflows have made the maintenance of the note coverage limit ever more difficult and finally impossible. The position of the the big banks was weakened. The closure of the Damstädter und Nationalbank ['Danatbank'] finally created a run on all banks and saving funds and led to the temporary closure and then extreme limitation of

payments of all money institutions.

“For the elimination of the panic there is only one path, the satisfaction of the need of means of payment, the payout of the deposits that are demanded back. The functioning of the credit organisation means, that the largest part of payments are settled through cheques, though transfers on the bank accounts, in short in a 'cashless' way. With a failure of the credit organisation all these payments must be carried out in cash, in legal means of payment [*gesetzlichen Zahlungsmittel*], that is in notes. The note replaces the credit means of payment. The amount of means of payment, the total circulation, is not increased, only one type of means of payment replaced by another. To fear inflation from this, when it is merely a compensation of a sudden, enormous contraction of the means of payment circulation due to the cessation of bank activity, is – ignorance.

“But the note shall after all in the panic not only replace a means of circulation of another type, but also serve the payout of assets [*Zurückzahlung der Guthaben*]. Now these assets, the deposits, were after all precisely the bases, on which the cheque, the entire cashless traffic rested; as long as they do not return, the means of payment resting on credit [that is deposits] remain contracted and the expanded note circulation necessary. But what happens with the notes, that are used for the discharge of deposits? The largest part is again locked up, hoarded. Insofar as this happens, the hamstered notes thus do not function as means of circulation, they can in general exert no influence on the price formation.

“Another part [of the notes] people will perhaps attempt to convert into foreign currency. But also here the restriction, the interest rate hike and the foreign exchange decree operate most inhibitively. A greater danger can here not arise; since the economy is under pressure from shortage of the Mark, necessary, to satisfy its obligations coming due.

“Finally perhaps goods are acquired. The notes flow however then to the seller of the commodities. Can he, under the credit restriction, under the fear, of having to repay already granted, now extraordinarily more expensive credit, do anything else with the notes, than keep them ready for his obligations, pay wages or raw materials and deposit the remainder in the bank, which he considers safe?

“The procedure, that is discussed here, has thus not in the slightest to do with inflation. Inflation arises and can only arise, when notes are printed for extra-economic purposes, for the need of the state. Here however it is about an economic

need, about the replacement of credit circulation by note circulation. The Reichsbank however has stalled, to utilise this only instrument. It has feared, to lower all too much the coverage limit, although the coverage ratio has nothing to do with the security of the currency. When in 1847 the credit crisis in England lead to panic, the government suspended on 25 October the three years earlier established, praised as panacea for all money crises Peel's Act, eliminated therewith the legal restrictions on the note issue, and in short time the panic was over. The same thing repeated itself ten years later, and again in November 1857 the bank law was suspended. And the same lesson is provided by the panics, that shook in 1907 the American and in 1927 the Japanese credit system. Had the Reichsbank acted according to this lesson, the closure of the Danatbank, the bank holidays and the run could have been spared from us. In any case the partial and disorderly domestic moratorium, which they signify, is no solution. For this situation cannot possibly continue for long. If the banks are to function again, then they have to satisfy the demands made, then they have to pay, and pay they can, so long as the credit traffic is disturbed, only with notes of the Reichsbank."[758]

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The collapse. The credit crisis in England

The annulment of the obligation of convertibility of the Bank of England is an event, whose full reach at the moment can only be guessed. Since the Napoleonic wars the Bank has suspended the convertibility of its notes only still in the world war. During the entire nineteenth century, during the successive revolutions, during the Crimean war and during the German-French war the English currency remained unimpaired. Now in the middle of a so called peace the Bank of England is driven to the annulment of the obligation of convertibility. The English currency is from today *a paper currency*, threatened by the at the moment extraordinary strong passivity of the English balance of payment.

The causes for this are very clear and were explained by us already before. The crisis in Central Europe and in particular the illiquidity of German short term credit hit the London finance centre most heavily and engendered there likewise *concern about the maintenance of liquidity*, meaning, the possibility to be able to repay at any time of desire the short term

[758] Hilferding 1931a, pp. 104–5.

borrowed money, that is primarily the American, French, Dutch and Swiss extraordinarily high assets [*Guthaben*]. England was however also hit in full severity by the *crisis in Australia* and *South America*, which rendered questionable or impossible the commitment of large interest payments, which England had coming [*zu fordern hätte*].

The concern about the English liquidity lead to a *rapid discounting of the foreign assets* by nearly all other banks. And the Bank of England lost in the last weeks *about four billion marks*, an unprecedented sum, a capital transaction that on such a scale in such a short time has not yet occurred in finance history. The run on Germany has repeated itself even more intensively, and with the same results.

The Bank has been empowered, to cease the sale of gold at a determined price. This means however the annulment of the decisive determination of the gold currency, whose essence after all consists therein, that anyone at any time for a pound note receives a for all time determined quantity of gold. The English government certainly adds the remark, that the obligations of the English government or of the English Bank, that are payable in foreign currencies, are not touched. This refers essentially to the debt of 80 million pound, whose French and surely also American part is to be fulfilled in francs and dollars. In the main however the English obligations are expressed in pound sterling, and their immediate convertibility and realisability on gold basis has become questionable. It is at the moment hardly foreseeable, how England could avoid similar consequences, as Germany at the occurrence of the same situation had to draw.

What this means however, is shown by a single consideration. Not only the English foreign trade, *but the predominant part of world trade is financed with pound credits.* The value of the pound sterling is at the moment problematic. The signifies however, *that the entire foundation, on which world export and import builds itself, is shaken*. The shock, that therefrom must spread itself to world production, would be enormous, if it were not at once cushioned.

Like already the occurrence of the German crisis, [and] a fortiori the collapse of the global English organisation of credit illustrates the *failure of the central bank administrations*, in particular the most powerful one, the *American*, which disposes over more than twenty billions, and the *French*, over more than ten billions gold (alongside perhaps seven billion foreign currencies). A part of this gold, in good time made available to the German Reichsbank and the German economy, would have in connection with the Hoover Plan stemmed the run on Germany. The prevention of the German crisis would have prevented the English one. Now the situation is extraordinarily exacerbated, and a multiple of the

amount, that would then have been necessary, must now be applied, to bring the international credit crisis to a halt and achieve its resolution.

The *stock exchanges* are closed not only in Germany, but also in the greatest part of Europe, and a terrible panic has gripped the capitalist world. The illiquidity of English finance will in the strongest degree reverberate first of all also on the *United States* and on *France*. The banks of these countries will attempt, to make themselves more liquid by collecting their claims, without being able to really achieve the goal. The central banks of the United States and France face now therefore the same problem in its entire gravity anew, *to ruthlessly and on the greatest scale mobilise the hitherto carefully guarded, in the cellars of the banks locked gold treasure, to master the credit crisis*. If they do not do it, then the English crisis eventually will very rapidly engulf New York and finally also most strongly affect Paris, even not to speak of the smaller European finance centres.

But whether they will do it, is an open question. Their hitherto policy with its superstitious clutching to every gram of gold does not leave all too great hope!

Nonetheless this path of immediate application of gold is the only one, that can rapidly solve the crisis. *Utopias of national and international inflation are entirely senseless*. Besides their economic impossibility and harmfulness they are *politically hopeless*, since the economic and therewith the political power of France and England[759] rests on the clutching to the gold standard. Not the pursuit of this utopia, but the deployment of gold, to repair the disturbed international balances of payment and effect the international evening out of payment, is the means, that most rapidly can bring the enormous credit crisis to a halt. But whether it will be really seized, before the United States and France themselves end up in acute payment difficulties, remains with the nature of the central bank leaders unknown.

For *Germany* in this moment perhaps two things can be said: *The enormously increased uncertainty worsens also the economic situation, and also Germany will strongly feel the disruption of the export financing, which today already faces great difficulties*. But on the other hand the German credit crisis, the Stillhalte[760] and reparation problem, stops being an isolated German question and becomes *part of the solution of the international credit crisis*, which tolerates no postponement, if the repercussion on the production in all countries is not to spark enormous social and political tremors. This *internationalisation* can *signify an easement*, because it shows, what pernicious effects economic and financial overburdening of a country must bring for the entire world.

For us socialists however this newest and greatest form of manifestation of capitalist

[759][Probably Hilferdingmeant here the United States.]
[760][The Standstill Agreement, to freeze German payments.]

anarchy, this failure of the credit organisations of the world, a world, which from the greatest wealth once again has engendered greatest poverty, is the new proof for the necessity of a different superior organisation of the economy!

Chapter Thirty

The Law of the Tendency of the Rate of Interest to Fall (1923)

Wolf Motylev

1.

Part V of the third volume of *Capital*, devoted to the analysis of interest-bearing capital, and studying the problems of the theory of credit, is one of the least prepared parts of *Capital*. Engels says in the preface to the third volume, that during the development of this part Marx caught a heavy bout of illness and, therefore, this part in the manuscript represents 'only the beginning of an elaboration — often just a disorderly mass of notes, comments and extracts'. In the by Engels ordered form the part consists in the significant sections of different quotations, followed by short notes of Marx; the other section, although it has more systematic nature, too represents an unfinished rough draft. Despite, however, the absence in the part of a coherent and comprehensive theory of credit, – its individual elements are given in a more or less prepared form. Even for undeveloped issues there is a mass of valuable comments, outlining the path to their solution and development. Moreover, this part comprises numerous ideas about the tendential developments of banks and credit, brilliantly foreseeing such phenomena, which took place only after some decades.

The task of developing the theory of credit and illuminating the phenomena of modern

capitalism, as is known, Hilferding tried to fulfil in his *Finance capital*. This task he succeeded only by and large. This was, however, enough for his book to be declared the 'natural continuation' of Marx's *Capital*.

Meanwhile, Hilferding in this book was not satisfied with the further development and continuation of Marx's *Capital*, but tried in a whole series of questions to 'correct' Marx. These 'corrections' did not met enough critical attitude from the side of Marxist theorists. The broad Marxist audience, inclined to a respectful relation towards Marxists, reacted to the 'corrections' even less critically. This credulity is enhanced by the fact that Hilferding clothes his 'corrections' in Marxist phraseology and, moreover, formulates them en passant. The widespread distribution of *Finance capital* and recognition of it as 'continuation' of Marx's *Capital* – makes a thorough critique of all 'corrections' of Hilferding especially necessary. This is even more necessary since they are not so unimportant and harmless as it may seem. In his review of the book of Hilferding (Kautsky 1911a) Kautsky limited himself, for example, only to a brief critique of the theory of money of Hilferding, indicating, that a more detailed analysis, he considers unnecessary, because on the present study of the author it did not have any influence. But soon Hilferding in a new article (1912) applied his theory of money to solve the most urgent problems of that time – the problem of the high cost of living. Kautsky became convinced that the 'correction' is not so harmless and hurried to submit the theory of money of Hilferding to thorough analysis.[761]

If the 'correction' of Hilferding on the theory of money underwent in the end an analysis and critique, then his correction to the theory of the interest rate of Marx, – his objection on the question of the tendency of the rate of interest to fall – did not call forth thorough criticism from the side of Marxist theorists. Meanwhile, this 'correction' of Hilferding in no less degree contradicts both the objective processes and facts, as well as the ideas, developed by Marx in the third volume of *Capital*.

In part V Marx gives a detailed analysis of the nature of interest, its relationship to profit and the tendency of its development. Marx defines the dependence of the money market, and hence also the interest rate, on the commercial-industrial conjuncture and the development of commercial and bank credit, on the state of the trade and payment balance and the exchange rate, on the quantity of the means of circulation, on the level of the rate of profit, on the level of commodity prices, and so on.

In the process of studying these issues Marx stipulates the law of the tendency of the rate of

[761]Kautsky 1912. That article represents a perfect analysis of the theory of money of Hilferding and also sheds light on a problem of the measure of value under modern paper-money circulation. It has been translated [by Motylev himself] into Russian and printed in the journal *PZM* (*Under the banner of Marxism*) No. 11-2, 1922.

interest to fall. This tendency follows, according to Marx, from three sorts of circumstances: 1) the growth of the rentier class with the development of capitalism; 2) the development of the credit system and the progressive concentration by banks of all free funds; 3) the tendency of the rate of profit to fall. All these factors affect the supply and demand of loan capital. Hilferding disputes, however, the accuracy of this law.

The law of the tendency of the rate of interest to fall Hilferding considers a 'dogma'. In his opinion, no theoretical considerations nor empirical material show the tendency of a 'constant' and 'invariable' fall of the level of the interest rate. The theoretical objections of Hilferding are strikingly poor. Let us give their formulations in full.

First objection:

> The rate of interest would show a downward tendency only if it could be assumed that the relation of the existing gold stock to the demand for loan capital is always becoming more favourable, that is to say, that the gold stock increases more rapidly than the demand for loan capital. But if we consider only developed capitalist systems, such a tendency for interest rates to decline steadily [constantly] cannot be established. Nor can it be postulated theoretically, because simultaneously with the increase in the gold reserve and in the minimum of circulation there is an increase in the amount of gold entering circulation in a period of prosperity.[762]

Second objection:

> A fall in the rate of profit would involve a decline in the rate of interest only if interest were a fixed part of profit; but this is not the case. At most, a decline in the rate of profit means that there has been a reduction in the theoretical maximum level of interest, namely the total profit. ... The rate of interest is not determined by the rate of profit, but by the stronger or weaker demand for money capital resulting from variations in the rate of development, and the tempo, intensity and duration of periods of prosperity.[763]

Hilferding attempts to confirm these theoretical considerations by an analysis of the table of the average interest rate in the four major European banks from 1852 until 1907. Let us postpone, however, for now the review of this table and try to understand the issues

[762]Hilferding 1981, p. 103.
[763]Hilferding 1981, pp. 103, 392.

theoretically.

2.

First of all, it is necessary to find out, in what the fall of the interest rate may actually be manifested and how it can be detected. The whole reasoning of Hilferding testifies to the fact that he understands the fall of the interest rate partly in the sense of a falling of the upper limit of the fluctuations of the interest rate. In the first objection quoted by us he indicates, that in the period of boom the gold reserves are reduced, – wanting with this to say that in such periods the interest rate will always greatly rise. If even that was true, it would prove nothing at all, as the issue is not about the level of the interest rate in one or another individual period of the industrial cycle. When we talk about the tendency of the rate of interest to fall, the question is about the tendency of the average rate of interest. 'In order to find the average rate of interest, – says Marx – 'we have to calculate the average interest rate *as it varies over the major industrial cycles*'.[764] Thus, swings up and down by themselves still do not prove anything. On the contrary, Marx in part V in detail points out the inevitability of changes of the interest rate depending on the periods of the conjuncture. In the period of stagnation the interest rate falls extremely low: in the period of growing revival also the flourishing of the interest rate increases; in the period before the crisis, and in the period of the crisis, it is high, at the instant of crisis often exceeding even the profit level.[765] And yet, the average level during a large industrial cycle can be in decline, if during this cycle the interest rate was close to the lower limit or average level of fluctuations of a longer lasting time, than in the previous cycle, or if the lower limit of fluctuations decreases in comparison with the previous cycle.

In the first objection quoted by us and in the reasoning, preceding it in the text, Hilferding speaks not about the relation of demand for loan capital to the supply of it, but of the relation of demand to gold reserves; that is to the means of circulation. He proceeds with this from the following statement of Marx: 'Variations in the rate of interest ... depend on the supply of loan capital (all other factors, the state of confidence, etc., taken as equal), i.e. of capital lent in the form of money, in metal or notes; as distinct from industrial capital that is lent as such, in the commodity form, by commercial credit among the reproductive agents themselves'.[766]

[764]Marx 1981, p. 484, our emphasis.
[765]At the same time, however, the tendency to fall of the upper limit of fluctuations of the interest rate is undoubtable.
[766]Marx 1981, p. 631.

Does it follow, however, to perceive in this quote the dependence of available loan capital on the *quantity* of means of circulation? Certainly not! Marx expresses here only that idea, that commercial (circulation – in Hilferding's expression) credit under its normal condition and development (with this the sense is indicated, that the soundness of credit is supposed; for Marx it is no less clear than for Hilferding, that every violation of commercial credit increases the need for bank [capital – in Hilferding's expression] credit), does not influence the interest rate, that the level of the latter depends on the demand and supply of loan capital in excess of circulation credit.

The by Hilferding posited close dependence between the supply of loan capital and the quantity of the means of circulation or payment does not stand up to criticism.

> The volume of this loanable money capital, – Marx says, – is still different from and independent of the quantity of money in circulation. .... The very possibility that large sums will be deposited while the amount of means of circulation is relatively small depends entirely on: (1) the number of purchases and payments that the same piece of money performs; (2) the number of return migrations in which it comes back to the banks as a deposit, so that its repeated function as means of purchase and payment is mediated by its renewed transformation into a deposit.[767]

Thus, between the supply of loan capital and the quantity of means of circulation there is not that close dependence, which Hilferding tries to posit. Money is only an instrument of credit, a means to transfer capital from the hands of lenders into the hands of borrowers. A small amount of money can serve a large number of such transfers of capital, if the velocity of the circulation of money as means of payment and purchase is great. At the same time, parallel to the growth of commodity circulation, grows in fact also the gold reserves and the quantity of means of circulation. Furthermore, the development of cheque circulation and an improved settlement system reduces the need for money, and that signifies – the dependence on the size of gold reserves and the quantity of banknotes.

Hilferding points out that in the period of high conjuncture circulation absorbs an additional amount of gold and that the rest of the gold reserves, which can be the basis for loans, decreases, and this drives the interest rate up. But it is quite obvious, that the period of high conjuncture is affected not by a lack of means of circulation, but by a lack of loan capital; the latter is only outwardly manifested in the lack of means of payment and purchase. It is not

[767]Marx 1981, pp. 631–2.

necessary, of course, to deny that in the period of high conjuncture and especially crises the interest rate, under the influence of the growth of the demand for capital, – increases and reaches always a considerable height. However this circumstance is not proof of the incorrectness of the law of the tendency of the rate of interest to fall, because, as we have already pointed out, it is not about individual periods, but about the average level during the course of a large industrial cycle. The dependence of the interest rate on the quantity of means of circulation was there, where there existed erroneous limitations and constraints on the issuance of banknotes. Indeed, Hilferding illustrates his considerations by examples of the monetary circulation of Britain and the United States, where such constraints occurred. But in England Robert Peel's Act of 1844, artificially constraining the issuance of banknotes, unbacked by metal, to the amount of 18.5 million £ in reality was neutralised by two circumstances. From one side, in times of acute financial crisis it usually was cancelled; so it was during the crises of 1847, 1857 and 1866. From the other side, the disadvantages of this constraint of emission policy were largely eliminated by the strong development in England of cheque circulation and the creation of an accomplished settlement system. During the last war Britain found a way that, without changing the rules of the issuance by banks of banknotes, allowed the Exchequer to issue additional paper money. As for the United States, the reform implemented there in 1914 of the monetary circulation removed the erroneous tightness of monetary circulation, having exacerbated the monetary crisis in 1907.

About a dependence of the interest rate on the quantity of means of circulation there can also be spoken in cases of outflow of gold abroad, depending on the balance of payments and the exchange rate; in such cases, the interest rate increases. However, such phenomena are typical only for individual periods and moments and in the volume of a large industrial cycle they rarely have a decisive impact on the average rate of interest. On the other hand, it is necessary to emphasise, that the outflow of gold is often a consequence of export of capital, so that here, it is not only a reduction of the amount of means of circulation, but also a reduction of the available loan capital. In this way, there is no reason to posit a permanent and close dependence of available capital on gold reserves, on the quantity of means of circulation. In most periods demand and supply of loan capital is established independently of the size of the gold reserves. One can, and should, therefore, speak of the relation of demand for loan capital to the supply of it, without dependence on the quantity of means of circulation.

3.

In order to establish the tendency of the movement of the rate of interest it is necessary first of all to find the tendency of the development of the demand and supply of loan capital.

Marx posits that the gigantic expansion of the reproduction process itself creates an increased supply of loan capital. 'But wasn't this gigantic increase in production itself the increase in capital, and if it created a demand, did it not create at the same time the supply, and at the same time also an increased supply of money capital?'[768] This augmentation of loan capital develops in two directions.

On one hand, with the growth of industrial capital grows also commercial (circulation in Hilferding's expression) credit, that is, credit that producers give to each other. This credit represents by itself credit until the completion of the process of circulation, and replaces for capitalists additional capital, which would have been necessary to them during the circulation period. While the process of production takes place smoothly and the produced commodities are realised within the normal period of circulation, all industrialists and merchants can safely carry out such mutual credit system. The representative of such credit transactions is the bill of exchange; the role of banks consists of the fact that they replace the circulating bills of exchange by circulating banknotes or cheques. The augmentation of bills of exchange is the basis for the augmentation of the quantity of banknotes or circulating cheques. The growth of commercial (circulation) credit augments in the same volume the absolute size of the demand and supply of money capital, without changing their ratios. Therefore, the growth of this credit may not affect the rate of interest. 'As long as the reproduction process is fluid, so that returns remain assured, this credit persists and extends, and its extension is based upon the extension of the reproduction process itself'.[769] Thus part of the growing demand for loan capital finds its satisfaction in the system of circulating credit, without the aid of additional money capital. Only in violation of regular production, under the appearance of disproportionality do breaks in the system of circulating credit begin and is born the need in corresponding amount for additional capital.[770]

On the other hand, simultaneously with the expansion of production the inflow increases of funds into the money market from such sources that are attempting the same expansion of

[768]Marx 1981, p. 553.
[769]Marx 1981, p. 614.
[770]The theory of commercial and bank credit developed by Marx in part V (Marx 1981, pp. 610–6), is of great importance for the understanding of the phenomenon of the money market. Hilferding replaces the names 'commercial' and 'bank' with the names 'circulation' and 'capital'. The scope of the article does not allow us to dwell on some controversial questions, connected with the theory of commercial credit.

production. To this relates primarily the sums of surplus value, profit, deposited over a certain period in the form of money, so long as they have not reached a magnitude, sufficient for productive application. With the growth of industrial capital grow also these sums; the increase in the size of enterprises, the size of fixed capital, increases the size of the minimum amount, at which capital can find a productive application and leads, as a consequence, to a longer lasting existence of these funds in the form of money capital. Further, the increase in size of fixed capital increases the absolute size of the sums deposited after each period of turnover to recover the worn-out part of the value of fixed capital and the duration of their existence in the form of money capital. Further, the growth of that part of the profit, which is spent by capitalists as income, is expressed in a periodically recurring and expanding accumulation, insofar as capitalists hold these funds in banks. Likewise increases the mass of capital, produced in many plants periodically, depending on the change of seasons. Finally, the sums of money also increase, which is always found fixed as current [bank] account, as current cash balance. Thus, we see, that if the expansion of production increases demand for loan capital, it at the same increases also its supply.

If we consider, moreover, the impact on the money market of the progressive increase of the rentier class and the size of their capital, as well as the impact of the perfection of the credit system and the concentration by it of all free funds, then it becomes obvious that overall (but certainly not in individual periods of the industrial cycle) the supply of capital grows faster than the demand for it. Marx quotes from Ramsey, clarifying the influence of the growth of the rentier class on the money market.

> For as a nation advances in the career of wealth, a class of men springs up and increases more and more, who by the labours of their ancestors find themselves in the possession of funds sufficiently ample to afford a handsome maintenance from the interest alone. Very many also who during youth and middle age were actively engaged in business, retire in their latter days to live quietly on the interest of the sums they have themselves accumulated. This class, as well as the former, has a tendency to increase with the increasing riches of the country, for those who begin with a tolerable stock are likely to make an independence sooner than they who commence with little. Thus it comes to pass, that in old and rich countries, the amount of national capital belonging to those who are unwilling to take the trouble of employing it themselves, bears a larger proportion to the whole productive stock of the society, than in newly settled and poorer districts. ... As the class of rentiers

increases, so also does that of lenders of capital, for they are one and the same.[771]

This process strengthens with the development of monopolies and joint-stock enterprises. To apply one's capital independently in production is possible only for owners of large capital.

In line with the growth of individual rentiers grow also rentier institutions and their capital, applied in the quality of loan capital. To this relate the capital of churches, monasteries, charitable and academic institutions.

No less important is the improvement of the credit system. So long as the credit system is insufficiently branched and poorly penetrates all corners of the country, so long as it does not enjoy sufficient confidence among the population, and is not linked adequately with industry and commerce, until then it does not concentrate all free money capital and therefore its supply on the organised money market lags behind demand. But insofar as the credit system permeates in all corners of the country, associates with industry and commerce, and with wide layers of the public, – it increasingly concentrates all free capital, savings, funds and in this way increases the supply of loan capital. Of great importance is also the degree of connectivity between the parts of the credit system, the degree of its centralisation. If between individual banks or individual areas there is no proper connectivity, then the free funds of the country are used irrationally. At the same time when in individual banks or areas there may be free capital, others may suffer a need for it. This occurs both in the form of differences in seasons, and in result of differences in periods of turnover. An appropriate connection between the parts of the credit system leads to the transfer of free capital and resources from individual areas and industries to others, which is tantamount to an increase of available capital. 'The accumulation of loan capital may take place without any genuine accumulation, by purely technical means such as the expansion and concentration of the banking system, saving on the circulation reserve or even on private individuals' reserve funds or means of payment'...[772]

Thus, a plurality of phenomena, occurring with the development of capitalism, creates the tendency of a faster growth in supply of loan capital, than demand for it, – the tendency of the rate of interest to fall.

The tremendous growth of own capital and deposit banks over the past decades is a confirmation of the theoretical considerations and assertions. If one compares balance sheets of German commercial banks with share capital of not less than one million marks for

[771]Ramsey quoted in Marx 1981, pp. 483–4.
[772]Marx 1981, p. 627.

the period 1886–1912, it appears that the number of such banks has increased by 220%, their own capital by 445.7%, other people's funds [*chuzhie sredstva*] by 849%, deposits by 1710.3%. In France for the period 1872–1909 the own capital of the three dominant banks increased by 440%, and other people's funds by 1021.7%. In England for the period 1890–1912 the own capital of deposit banks (without English ones) grew by 121%, deposits by 192%. In Russia for the period 1897–1912 own capital increased by 318%, and deposits by 620%. In France, for the period 1900–1910 deposits and current accounts in five major credit institutions increased from 2.2 to 5 billion francs.[773]

4.

If, together with the tendency of the rate of interest to fall, there was no tendency of the rate of profit to fall, – then the first tendency in the process of its development would have to had hit upon a series of counteracting factors. The fall of the interest rate at an unchanged or increased profit rate level would have meant a corresponding rise of the level of business revenue. But that would have caused an increase of demand for loan capital on the part of borrowers and the emergence of a desire of part of the lenders – for an independent productive application of their capital in order to obtain high entrepreneurial revenue in their favour.[774] As a result there would be some increase of demand for loan capital and some reduction of supply – and the interest rate would begin to rise. That is why for confirmation of the tendency of the rate of interest to fall, the by Marx established link between both tendencies and determination of the tendency to fall of the interest rate [by] the tendency to fall of the profit rate, has great significance.

> All other circumstances taken as equal, – says Marx, – i.e. taking the ratio between interest and total profit as more or less constant, the functioning capitalist *will be able and willing* to pay a higher or lower interest *in direct proportion to the level of his profit rate*. Since we have seen that the level of the profit rate stands in inverse proportion to the development of capitalist production, *it follows that the higher or lower rate of interest in a country stands in the same inverse proportion to the level of industrial development*, particularly in so far as the variation in the rate of interest

[773]See table in the article of Finn-Enotaevsky 1913.
[774]We write 'of part' because in some cases the growth of deposits and savings does not depend on the interest rate, in some cases the fall of the interest rate even reinforces the desire for accumulation. This is indicated by S. and B. Webb (See *Industrial democracy*, pp. 625–6). The Webbs exaggerated, however, the size of such cases and phenomena.

> expresses an actual variation in the profit rate. We shall see later on that this need by no means *always* be the case. In this sense one can say that interest is governed by profit, and more precisely by the general rate of profit. And this kind of regulation applies even to its average.[775]

With the indication that there is no necessity that the level of the interest rate *always* expressed the direct dependence on the level of the profit rate, Marx points out the circumstance that in individual periods of the industrial cycle the interest rate may change under the influence of other factors, diverged sharply with the level of the profit rate. Decisive is the state of the money market, under which the interest rate can vary even in the reverse direction to the profit rate's fluctuation. Thus, in the period of stagnation and crisis when the profit rate is lowest, – the interest rate is highest. Conversely, in the period of increasing revitalisation, when profit grows, the interest rate is low and grows very slowly. During crisis the interest rate rises sometimes even above the profit rate, since borrowers are willing to pay any interest rate if only to avoid bankruptcy. In the period of the depression the interest rate drops frequently to 0.5%. A high interest rate coincides with a high profit rate in the period of boom. A low interest rate with a low profit rate – in the period of depression.
The laws of variability of the interest rate in individual periods of the industrial cycle in dependence on the commercial-industrial conjuncture were elucidated by Marx in part V in great detail.
But if in short periods the rate of interest may strongly diverge with the rate of profit, then for the prolonged periods between them is established nevertheless a certain interplay and correspondence. Marx repeatedly emphasises that 'variations in the interest rate ... occurring over longer periods ... are dependent upon variations in the general rate of profit'.[776] Although Marx does not characterise the detailed mechanism of this dependence, it is not hard to figure out of what it consists on the basis of the ideas of the third volume of *Capital*. A high interest rate cannot exist for prolonged duration under a low profit rate, since the low business revenue would lead to a reduction of demand for loan capital, and hence, to a decrease in the interest rate. Conversely, a slightly low interest rate under a high profit rate would lead to an increase in demand for loan capital and increase the interest rate.[777]

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[775]Marx 1981, pp. 481–2. Our emphasis.
[776]Marx 1981, p. 631.
[777]These considerations apply, however, only to prolonged periods, to a whole cycle with a changing conjuncture. To short periods they are not applicable. But the matter is exactly about whole cycles. The following quote shows that Marx thought exactly like this about the mechanism of this dependence: 'If an

Therefore it is entirely obvious that with the presence of the tendency of the rate of profit to fall there exists also the tendency of the rate of interest to fall, even if one abstracts from the influence of all factors, outlined by us above.

After all what has been said, the erroneousness becomes apparent of Hilferding's position on the question of the influence of the tendency of the rate of profit to fall. Hilferding does not bother to bring any substantive proposition against the possibility of such an influence. He limits himself to a dogmatic assertion that the level of the rate of interest depends only on the greater or lesser demand for capital and is not determined in any way by the rate of profit. *But we have seen that the profit rate influences the interrelation of demand and supply of loan capital.* The assertion of Hilferding reveals only his theoretical thoughtlessness on the given question.

5.

Let us turn now to the consideration of the actual movement of the interest rate over the past decades by individual countries.

The first thing that attracts attention when reading the table of the movement of the interest rate, is the fact of considerable, and sometimes even huge differences between the interest rates by individual countries. In England in the early sixties of the last century the average official discount rate for a year varies annually on average from 2.5 to 3.5%, dropping even to 2% and exceeding 3% only in years of crises and wars.[778]

In France for the last 4 decades (until the last war) the average annual official discount rate fluctuates per year between 2% and 3%, surpassing for this period only 4–5 times 3%, and then only one tenth percentage. In Germany the average annual official discount rate fluctuates per year during this same period between 3 and 5%, rarely falling below. In Austria-Hungary during the same period the discount rate is rarely less than 4%. If we turn to Russia, then here the difference is even clearer: the average official discount rate per year for the 1860–1914 period ranges between 5% and 7%, almost never dropping below.

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inappropriately large number of capitalists sought to transform their capital into money capital, the result would be a tremendous devaluation of money capital and a tremendous fall in the rate of interest; many people would immediately find themselves in the position of being unable to live on their interest and thus compelled to turn themselves back into industrial capitalists' (1981, p. 501). Although this is stated on a different subject, the line of reasoning is the same.

[778]We will consider only the movement of official and private discount rate, that is rates which are levied by the central and private commercial banks for the discount of three and six months bills of exchange. Official and private discount rates represents themselves the fluctuation of all other interest rates. Fluctuations in the discount rate characterise in the majority of cases fluctuations of the interest rates in general.

For the bills of exchange for a duration of 9 and 12 months the discount rate fluctuates between 6% and 9%.[779] The difference in the interest rate level between individual countries, as we see, is huge. In the countries of 'old' capitalism the interest rate is low. In the countries of 'young' capitalism it is high. The 'younger' in capitalist development the country, the higher the interest rate. Hilferding will have to explain that this difference depends 'on the stronger or weaker demand for money capital resulting from variations in the rate of development, and the tempo, intensity and duration of periods of prosperity'.[780] But it is entirely clear that this explains absolutely nothing, because it raises a series of questions, which, on the basis of Hilferding's views cannot be answered. Why in the countries of 'old' capitalism is the interest rate low, and in the countries of 'young' capitalism – high? After all for Hilferding there is no tendency of the rate of interest to fall! Why in the countries of 'young' capitalism do capitalists prove able to pay such a high interest rate? On these questions Hilferding cannot answer, if he is not to renounce his views! Meanwhile, on the basis of the by us developed views of Marx all this is perfectly understandable. The countries of 'old' capitalism differ from countries of 'young' capitalism by a greater development of the rentier class and its capital, a greater concentration of free funds in banks, a lower rate of profit; all this leads there to a low interest rate. Conversely, in countries of 'young' capitalism free capital for the above outlined reasons is few, the credit system is not perfected, the rate of profit is high, – hence the high rate of interest. Can Hilferding deny that Russian capitalists, despite the high interest rate, get more business revenue, than the European ones, – in consequence of the high rate of profit? It is obvious that the high rate of interest could be kept only thanks to the higher rate of profit.[781]

The difference between the interest rates by country appears even greater if we turn from the official discount rate to the private one. Based on the views of Hilferding it is difficult to explain that striking fact, that in England and in France (before the war) the private interest rate was lower than the official one, whereas in Russia it was higher than the official one.[782] At the same time as in London and Paris the private discount rate fell to 1–1.5%, Russian private banks were charging 5–6% per year and above. Meanwhile this only confirms Marx's view. In the countries of 'old' capitalism private banks are closely related with certain groups

[779]Consolidated full table of the movement of the Russian official discount rate, see Jasnopol'skij 1914, part 1, appendix 1.
[780]Hilferding 1981, p. 392.
[781]The higher profit rate in countries of 'young' capitalism is due to lower organic composition of capital, the higher rate of surplus value, the existence of sale markets, and so on.
[782]See, for example, the tables, attached to the book of Suvchinsky 1912. In the tables are compared the non-official interest rate in Paris with the official ones in Paris, London, Berlin and Saint Petersburg for the period 1898–1909.

of rentiers and with certain industrial and commercial enterprises and derive their funds from them, – thanks the abundance of capital they can charge a low interest rate. The central bank in these countries often increases its discount rate in order to regulate the money market and monetary circulation: suspend export of capital, increase the exchange rate, and so on. On the contrary, in Russia private banks drew their funds partly from the State Bank and, paying to it for them a certain interest rate, needed themselves to charge, of course, a higher interest rate. This was due to the country's poverty of loan capital and the imperfection of the credit system. This was possible thanks to the high rate of profit. 'Differences between interest rates in different countries ... are conditioned ... by differences in profit rates and in the development of credit'.[783]

We see, thus, that the difference in the interest rate between countries brilliantly confirms the view of Marx and refutes the 'correction' of Hilferding. The fact of the fall of the rate of interest being dependent on the degree of capitalist development of the country, which we observe when considering the statistics of the interest rate over a spatial range, – only reflects and confirms the existence of the tendency to such fall over time.

Let us turn now to the consideration of the table of the interest rate movement, [by] which Hilferding attempts to confirm the correctness of his views.[784] This table gives in four vertical columns a picture of the movement of the average official annual discount rate in four major European banks from 1852 to 1907. This table deserves attention. Oddly enough, it decisively disproves the view of Hilferding. A careful viewing of the table creates a puzzling question: how can Hilferding not see that this table is a striking *confirmation* of the tendency of the rate of interest to fall?! Let us begin with the fact that a simple comparison of the interest rate for the four countries with obviousness reveals that difference about which we have spoken above. Hilferding, however, does not notice it. He did not mention a word about this difference. Meanwhile, as we have seen, it goes by far not in his favour and if he had paid attention to it and raised the question of its cause, this could have lead him to somewhat different conclusions. Not better either, however, for Hilferding's case is the nature of the movement of the interest rate in this table by vertical rows. In England, for example, until 1867 the annual average interest rate fluctuates very sharply: from 2.5% to 7.8%. After 1866 the numbers 7, 6, 5 are already not found in the table. 4–4.5% occurs only in years of crises. In other years the interest rate ranges from 2.5% to 3.84%, but is usually equal to 2% or 3%. In Germany until 1885 the number 3 in the table is almost never encountered.

After 1885 the number of 3% with a fraction prevails and only in years of crises the interest

[783]Marx 1981, p. 631.
[784]Table in Hilferding 1981, pp. 390–1.

rate rises to 5% with a fraction. In Austria until 1880 the table is dominated by 5% with a fraction. After 1880 5% is little found. There dominates 4% and 4% with a fraction and even since 1902 there dominates 3% with a fraction. It is curious, however, that Hilferding himself brings a quote from the article by Dr Schwoner apropos these tables, where the latter notes all these facts of the decline of the interest rate and the pushing of the boundaries of the interest rate down. Schwoner's statement in the first sentence of this quote, that in the table 'no definite tendency, upward or downward, is demonstrable' (p. 392), strongly contradicts not only the content of the table, but also his own, Dr Schwoner's, further reasoning. Hilferding gives the following consolidated table by decade, compiled by Schwoner on the basis of the first table.

	Bank of England,	Bank of France,	German Reichsbank,	Austro-Hungarian Bank,	Overall average
1897-1906	3.52	2.85	4.28	4.05	3.67
1887-1896	3.04	2.71	3.59	4.21	3.38
1877-1886	3.19	2.96	4.11	4.26	3.63
1867-1876	3.25	3.89	4.34	4.85	4.09
1857-1866	4.28	4.48	4.83	5.06	4.79

This table, like also the first, brilliantly confirms the law of the *tendency* of the rate of interest to fall. Schwoner himself is forced to admit, and indeed it is impossible to deny, that until 1897, the interest rate invariably falls. On the table for the vertical rows this is detected with clearness. As for 1897–1906, Schwoner correctly notes that during this decade the average was 'higher than in the preceding two decades, but far below the average during the first twenty years of the financial and industrial upswing, 1857–76'.

What, however, explains the increase of the interest rate for the decade 1897–1906 and does it contradict the law of the tendency of the rate of interest to fall? With that question clearly has been revealed the narrowness and unscientific nature of the views of Schwoner and Hilferding! Hilferding, having explained in detail in the eighteenth chapter of *Finance capital* the influence of conjuncture on the interest rate level, – could not, however, understand the connection of the movement of the interest rate with the cyclical development of capitalism in recent decades. Capitalism undergoes in its development two types of cycles: large cycles, covering about 50 years, – and within the frames of a large cycle, – small cycles, spanning 7–11 years. Every large cycle is divided into two periods (in 20–30 years); the first is characterised over all by commercial and industrial boom; the second – depression. Developing on the background and within the limits of those periods of the large

cycle, small cycles do not significantly violate this general character of each period. The first large cycle lasted from 1789 to 1849, wherein until 1809 the first period lasted, after 1809 – the second period, characterised [by] depression. The second large cycle lasted from 1849 up to 1896, – wherein until 1873 developed the wave of rising conjuncture; from 1873 to 1896 – the wave of declining conjuncture. The third great cycle began with 1896 and its first period, characterised by a wave of rising conjuncture continued until the crisis of 1920 and now we have entered in a strip of declining conjuncture.[785]

But inasmuch as the national economy develops cyclically, insofar, obviously, a continuous and constant fall of the interest rate is impossible. In the first period of the large cycle, characterised by a rising wave, the interest rate should be higher than in the preceding second period of the previous cycle, characterised by depression. *The tendency to fall of the interest rate may and should appear in the fact that in the first period of one large cycle the interest rate is lower than in the first (but not the second) period of the previous cycle.*

These ideas brilliantly are confirmed both by the table and the reasoning of Schwoner. The first two decades of the table (1857–76) relate almost entirely to the rising period of the second cycle. The second two decades (1876–96) belong to the second period of this cycle, characterised by depression. The last decade of the table (1896–1907) relates to the upward period of a new large cycle. And, indeed, during the second two decades the interest rate is lower than in the first. In the last decade, the interest rate is higher than the previous two, but lower than in the first two decades. *Thus, the table appears understandable and fully supportive of the tendency of the rate of interest to fall, if the cyclical development of capitalist economy is taken account of.*[786]

6.

The narrow, unscientific and anti-Marxist approach of Hilferding to the question manifests

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[785][On large cycles, see: Prof. Kondratiev. 'The world economy and its conjunctures during and after the war', part 5. The law of large cycles, despite its undeniablity, theoretically has not yet been developed. In that fact, that the movement of the interest rate confirms it, we see a palpable proof of its correctness.
Jacob van Gelderen (1913, p. 35/37) too remarked Hilferding's failure to see the wave-movement of the interest rate: “Incidentally, it must be pointed out that, in his reflections on, the development of the interest rate, Hilferding did not notice the threefold, wave-movement demonstrated here.”
Motylev's reference to Kondratieff brings to mind also the wave-movement of the price level, that is. both the price level and the interest rate moved upward in the 1896–1913 period. The phenomenon of their co-movement is referred to in mainstream economics as the Gibson paradox.]

[786]After submitting this article to print we were able to get acquainted with the thorough article of Dr Vogel on the movement of the interest rate (Vogel 1916). We use the proofreading, to note, that the table cited in the article of Vogel confirms our reasoning and conclusions. Vogel commits, however, a number of theoretical mistakes.

itself in the fact that he is looking for a 'constant' and invariable' fall of the interest rate. Meanwhile, concrete reality is complex. Along with tendencies and forces of one direction there can take place also the opposite, counteracting ones. Given the presence of such counteracting forces, Marx also spoke only about a 'tendency' to fall of the interest rate, indicating therewith, that the fall of the interest rate will come up against a number of counteracting factors, which can slow down this fall and even temporarily turn and reverse the movement. Similarly Marx reasoned with the formulation in the first[787] part of the third volume of *Capital* of the law of the tendency of the rate of profit to fall. Marx says there that there are 'counteracting influences at work, checking and cancelling the effect of the general law and giving it simply the character of a tendency, which is why we have described the fall in the general rate of profit as a tendential fall'.[788] Having established and characterised in the thirteenth chapter 'the law as such', Marx moves therefore in the fourteenth chapter to the study of 'counteracting factors'. Of such 'counteracting factors' there are not a little also with the tendency of the rate of interest to fall. To this relate, first of all, the very fact of the cyclical development, which periodically creates the upward tendency of the interest rate. Further to this relate: the slowness of the fall of the rate of profit, wars, mistaken monetary legislation, unfavourable rate of exchange, etc. Finally, – and this is perhaps one of the major counteracting circumstances, – countries of old capitalism, in which must manifest the reality of this law, offer the world markets loan capital. Demand for it represents not only, and often not much, their own economy, as that of all the countries of 'young' capitalism. It would seem that demand, thanks to this, should exceed supply and the interest rate would have to be always at a high level. If, in spite of this, the table shows a fall in the interest rate, this is an obvious and undeniable confirmation of the correctness of the law. Only on the basis of the law of the tendency of the rate of interest to fall can one understand why the interest rate in these countries is low, despite the huge demand presented to them by young countries.

As for the counteracting influence of war, it was found particularly strong in the last war. Thanks to the huge demand for loan capital for military needs, the discount rate increases in all western European countries, including Britain and France – to 5%, and steadily is kept at this level during the whole war. The huge debt of all European states, colossal destruction in central Europe and the depletion of capital from the time of the war – continues to keep the interest rate at a high level also after the war. It reached a particularly high level during the crisis of 1920. After the crisis the interest rate begins to fall and at times reaches pre-war

[787][Probably an error, should be third part.]
[788]Marx 1981, p. 339.

levels. But the marked effects of the war will still for a prolonged time prevent the reduction of the interest rate level, despite the fact that we entered the second period of the large cycle.[789]

The harmfulness of the 'correction' of Hilferding clearly was stated in the final paragraph of his reasoning. Its application led to the distortion and obscuring of the actual process. Let us give this paragraph in full.

> In a developed capitalist system, the rate of interest is fairly stable, while the rate of profit declines, and in consequence the share of interest in the total profit increases to some extent at the expense of entrepreneurial profit. In other words, the share of rentiers grows at the expense of productive capitalists, a phenomenon which does indeed contradict the dogma (!!) of the falling interest rate, but nevertheless accords with the facts. It is also a cause of the growing influence and importance of interest-bearing capital, that is to say, of the banks, and one of the main levers for effecting the transformation of capital into finance capital.[790]

First of all, we found that 'in a developed capitalist system' the interest rate level 'falls' not less, than the profit rate does. But even if Hilferding would be right in this, then, contrary to his opinion, this phenomenon could not continue long and would soon be replaced by the reverse direction of movement. And indeed, a high interest rate under a low profit rate also decreases, as a result of the fact that the business revenue would have caused a withdrawal of capital from production and its transformation into loan capital. There would have been received an excessive supply of loan capital under a reduced demand. All this would inevitably lead to a fall of the profit rate, to a decrease in the 'share of rentiers', to the reverse conversion of part of the loan capital into productive capital. In order to explain the reasons for the growth of the supply of loan capital and the transformation of capital into finance capital, there is no need for such cheap, – strained explanations. The reasons for these phenomena were clarified in detail by Marx in part V, without the help of this 'explanation'. The actual reasons for conversion of capital into finance capital was adequately revealed by Hilferding himself fully and in detail in his book.

As for the revenues of the idle capitalists, they grow, despite the fall in the rate of interest. The *rate* of interest falls, but what grows is the *mass* of revenue, obtained in the form of

[789]On the movement of the interest rate during and after the war see: 1) the above noted book of Kondratiev; 2) 'The world economy in the time from 1913 to 1921', statistical yearbook, edited by Fal'kner 1922.
[790]Hilferding 1981, pp. 103–4.

interest, – due to the growth of the size, the mass of loan capital. This circumstance makes possible the growth of the class of rentier, idle capitalists, despite the fall of the interest rate. The assertion of Hilferding in this paragraph, that the weak variability of the interest rate under the falling profit rate is 'also a cause of the growing influence and importance of interest-bearing capital, that is to say, of the banks', does not remain isolated and negatively affected his subsequent theories. Throughout all his book there are two kinds of reasonings on the formation of finance capital. In some cases he considers finance capital as a merger together of industrial and banking capital, wherewith 'it is always the superiority of capital resources [power, *Kapitalsmacht*], and particularly disposal over freely available money capital, which determines economic dependency within a credit relationship',[791] – but in any case the concentration of industry 'is the ultimate cause of concentration in the bank system'.[792] Predominating, however, in Hilferding is the other theory. He claims that in the process of capitalist development the preponderance is on the side of the banks. While the bank possesses capital in the form permanently adapted to operation, – the capital of enterprises is fixed in the factory and cannot be arbitrarily removed from it without loss. On the other hand, industry uses an ever increasing amount of other people's money [*chuzhimi sredstvami*] and can obtain it only from the banks. In light of this the banks subordinate industry to themselves, and the merging of bank capital with industrial capital takes the form of the economic subordination and absorption of the second by the first. Both types of reasoning are interwoven in the book and the whole presentation of this question carries therefore a vague and contradictory character.

Meanwhile, it is unquestionable that the second type of theory is wrong.[793] Hilferding himself gave over the course of the book enough material for its refutation. And indeed, the corporatisation of industry destroyed the fixedness of industrial capital and makes it mobile and ready for operation. On the other hand, that circumstance that the supply of capital grows over all faster than demand, generates a constant interestedness [concernment] of banks in the application of this capital and alters the balance of power in favour of industry. Thus, it is impossible to assert that the preponderance moves to the side of the banks. In each concrete case it depends on the degree of power of both sides. Finance capital cannot be

[791]Hilferding 1981, p. 95.
[792]Hilferding 1981, p. 98. chapter five
[793]On the fallacy of these theories of Hilferding particularly strongly pointed out in his works Finn-Enotaevsky. See his works: 1) *Sovremennyj kapitalizma* 1913; 2) *The economic system of Karl Marx* [1922]; 3) *Modern economy of Russia*. With the objections of Finn-Enotaevsky we, however, do not agree in everything. To the incorrectness of these arguments of Hilferding has pointed also I. Stepanov in the foreword to the latest (1923) edition of *Finance Capital*. To a refutation of these theories of Hilferding also is dedicated a yet unpublished work of Elkon Goldenberg.

identified with banking capital. It is a fusion of banking capital together with industrial capital. At a certain stage of development of capitalism there can take place in some countries a preponderance to the side of the banks, – but, with the transition of capitalism to the highest stage, the preponderance, under the fusion into finance capital, turns out to be, in most cases, on the side of industry.

Thus, also in this reasoning of Hilferding there is an error, connected in part with his erroneous denial of the tendency of the rate of interest to fall.

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